

R O U G H D R A F T

Senate Committee on Governmental Organization

Roderick D. Wright, Chair

Examining the Public Policy and Fiscal Implications Related to the Authorization of Intrastate Internet Poker in California

**Tuesday, February 9, 2010
State Capitol, Room 4203**

SENATOR RODERICK D. WRIGHT: ...with our informational hearing. I'll be the referee. I want everybody to obey my commands at all times. There will be no saving by the bell, except after Round 10. After Round 10, you will be able to be saved by the bell. No rabbit punches. And again, obey my commands at all times. (Pause)

Okay. I'm going to give a couple more minutes for our members to get here. At this morning's presentation, the part of Steve Rittvo will be played by—Mr. Rittvo got stuck in snow in Washington, D.C., so he will not be here this morning. Again, as you can see from the agenda, we have kind of an ambitious agenda, but I think it's necessary for the scope of what we're trying to do. We're going to schedule to try to have approximately a 30-minute break, and we hope we can wrap up by about 4 o'clock. Now given the nature of what we're doing, we're going to set up a little pool as to what time we get out. (Laughter) You know, depending on who wins the pool, maybe we can give the money to somebody's charity. But you can't filibuster in order to extend the time if you bet on one side or the other.

I want to ask some of the witnesses if you would—and I know many of you have statements. If your statement is written, if you'd please give it to the

sergeant because we're going to form kind of a compendium of those things that were said for later handout, but it's not necessary for you to come and say the same thing that someone has already said. So if it's already been said, you can kind of say, he just said what I was going to say, and that's cool. You know, no offense will be taken if that's what you do.

Again, we're going to get started probably in five minutes. I'd like to get just a couple of other members in. You know, they were surprised we actually did start on time but we're going to try to do that. Those members of the first panel, if you would come forward and have a seat up because, as soon as we get going, we're going to crank that up.

Mr. Soderborg, Mr. Eadington, Mr. Millar, Mr. Catania, Mr. Derossi, and we'll just get you guys queued up. Again, Mr. Rittvo will not be here today. He is stuck in snow back East. So because of that, we will crank up for him. Again, I will open with a brief opening statement and then we'll get right to the panels for the people who were betting long that we're still going to try to keep on time.

As a matter of fact, what I think I'll do, gentlemen, if it's all the same, I'm going to just go ahead and do the opening. Again, because this is an informational hearing, a quorum is not necessary because we're not voting on anything today. So I'm going to go ahead and get us started. I'm going to open and then we'll go right to the witnesses.

Let me say a couple of things at the outset. I know we've got people who have traveled from Europe. We've had people who've traveled from across the country and some people who were trying. We do have an award for the people who've come from the furthest. Right now, I think Sweden is in front. So if anybody's come from further away than Sweden, let them be recognized now. But right now, the Swedes have the trophy for people who've come the furthest. For those of the general public or watching on CalChannel, again, this is will be available if you want to get a copy.

The purpose of the hearing today is to establish a framework by which the legislature can look at Internet poker. And I want to make clear that this is

not a referendum on anybody's proposal today because, as of present, there is no proposal before this committee or any committee in the legislature. There certainly are some ideas floating around, and this isn't for or against anybody's idea. So I mention that because I've heard discussions where people said I like this or that about this guy's proposal. This is not about anybody's proposal in particular. What we're talking about is Internet poker. We're trying to identify what would be the best course of action for the state of California, so we're trying to actually educate ourselves as to what makes good sense.

There are a number of fiscal implications. There are discussions as to what's legal; there are things as to what's not legal, whether or not it violates exclusivity. I could go into a number of issues that I hope we examine today. I've read some of the material from some people who said, well, this is illegal. Clearly, whatever it is we do, it's probably going to end up in court. So Judge Wapner will be the ultimate decider of what gets done and what does not.

We'll also be exploring what's the best method to proceed so there are a number of things, some of which, I'm sure that the staff of the committee and I and other members have not even begun to consider. So that's why we're here and, again, this is not an opportunity for people to level, you know, issues at other folk, and I know that there are longstanding wars that people have had and people have been on this side or that side. This ain't the place to do that. So if you're going to do that, as usual, that takes place outside. So, you know, if you're going to have a fight, you have to go outside and do it, although I do referee. I only do that on Wednesdays. So if you want me to referee the fight, it has to be on Wednesday.

Again, let me welcome all of the people who have come—the members of the public, people who are going to testify on panels, members of the California gaming industry for your being here this morning, and let me welcome the first panel, and I think we'll just go ahead and get started because we have such a long day and I don't want to influence the betting pool by starting late because we are trying to make that 4 o'clock cutoff. So thank you.

And Senator Harman, do you have an opening?

SENATOR TOM HARMAN: I think you've pretty much covered it, Mr. Chairman. I'd just assume, go ahead and start the hearing.

SENATOR WRIGHT: Okay. Well, let me welcome our first panel. This panel is on background and the relative issues to Internet poker. Since it is all guys, I can say, gentlemen, welcome aboard.

And Mr. Soderborg from the Legislative Analyst's Office, if you would start us off. Did I pronounce that right?

MR. DREW SODERBORG: That's correct, yeah.

SENATOR WRIGHT: Okay. Thank you.

MR. SODERBORG: Mr. Chair, Members, Drew Soderborg, Legislative Analyst's Office.

If you turn to the first page in the handout we've distributed, you'll see a discussion of what federal law currently allows with respect to online gaming. Under the Federal Unlawful Internet Gambling Enforcement Act of 2006, it is generally unlawful to place or receive gambling bets through the Internet. However, the act allows states to authorize online, intrastate gambling under certain conditions. For example, the type of bet or wager must be authorized by state law and cannot violate certain federal laws. In addition, rules and regulations must be adopted to prevent minors or non-state residents from participating in online gambling. At this time, we know, however, there are bills pending in Congress to legalize online gambling across all the states which would likely impact the revenues that states could obtain from legalizing intrastate, online gambling.

If you turn to the next page in your handout, you'll see a discussion of some of the broad categories of areas that we would feel would influence how much revenue the state could achieve from authorizing online poker.

One of the first issues that we feel would impact the level of benefit the state would receive from authorizing online poker would be the possible legal issues regarding tribal-state compacts. Another important factor would be the details surrounding how legal poker websites would be implemented in California. Another important factor would be the number of people who would

play online poker, as well as the amount those individuals would wager on a legal website. And finally, we feel that it would be important to note the extent to which legal websites are able to capture monies that are currently being wagered on illegal websites.

If you turn to the next page in your handout, we have a discussion of the possible legal issues regarding tribal-state compacts.

The existing tribal-state compacts that have been ratified by the legislature require the tribes to make payments to various state accounts. For example, the compacts ratified in 2003 and after require tribes to make annual payments to the state which are then deposited in the General Fund. The governor's budget for 2010-11 assumes the General Fund will receive \$365 million in revenue from these tribes in the budget year.

Also, these compacts contain provisions limiting the state's ability to authorize certain types of gambling that could compete with tribal casinos. These compacts may allow the tribes to stop making some payments to the General Fund if the state authorizes certain types of competing gambling enterprises.

There could be legal challenges that poker websites violate the above provisions in tribal-state compacts if online poker were approved in California. If such challenges were upheld, the state could lose hundreds of millions of dollars in revenue annually. Thus, the legislature should work closely with the Office of Legislative Counsel and other legal experts to assess these risks if it wishes to consider proposals in this area.

If you turn to the next page in your handout, you'll find a discussion of some of the specifics of how implementing poker websites would impact the level of revenue the state could receive.

One of the primary factors in how much revenue the state would generate is what portion of the gross revenues it would receive from the legal website operators. Given the state's fiscal difficulties, one goal could be maximizing the benefit the state would get from such operators. On the other hand, it's important to note, that if the state were to take too large a share and

the operators weren't allowed to retain enough funds, they might not be able to effectively compete with illegal websites. For example, they may not have enough funding left to pay for marketing or player incentives.

We also note that the state would incur regulatory costs to prevent unauthorized users from playing on legal poker websites. In addition, we note that it's not clear what specific steps individuals in California would need to take to be able to play on legal poker websites, such as providing proof of residency or paying registration fees. If these requirements were extensive, however, they could represent a barrier to player participation.

We also note that the number of websites would be important because, although the existence of multiple legal poker websites within California could promote competition, having too many sites could result in each site not having sufficient players to facilitate poker games.

Finally, we'll speak to some of the issues surrounding the tax revenue the state could get from a poker website. The website could be designed to make it easier to collect income taxes on net winnings. Currently, players using illegal websites have little incentive to report gambling winnings for tax purposes. The state could require that websites report such tax information. However, this could deter some players from using legal websites. We also note that the state could also collect taxes from the operators of legal poker websites as well as their employees.

If you turn to the next page in your handout, you'll see a discussion of some of the various factors that we would, we feel would influence how many people would be willing to participate in legal websites.

The first is the cost of play. If the cost of playing on legal poker websites was greater than the cost of playing on illegal websites, due to taxes and fees paid by the players, there could be a fiscal disincentive to play and wager similar amounts on legal websites. On the other hand, unlike illegal poker websites, the legal websites would be able to provide players with a greater sense of security as well as comfort in knowing the fact that they would not be engaging in an illegal activity. However, many of the existing illegal websites

offer financial incentives to retain players. For example, some sites offer bonuses to players that they can only collect after playing a predetermined number of hands. This could make it more difficult for a new California online website to capture a share of the market in the near term. The state, however, could also authorize similar incentives for its games. A final factor we note is that legal poker websites would have to compete with existing illegal websites that have little or no limits on the types of games they can offer.

If you turn to the final page of your handout, you'll find a discussion of the fact that the source of the gross revenue to the legal website would affect the total revenues that the state was able to gain from a legal website.

First, we consider state revenues from redirecting, wagering from illegal websites. Several studies estimate that illegal websites receive roughly \$300 to \$400 million in gross revenue from Californians participating in online poker. While it is not known how many current California players would switch from illegal websites, the state could gain new revenue by redirecting wagering from illegal websites to legal websites. However, revenue generated from existing players betting more than they otherwise would or from individuals who currently do not play, starting to play, would be offset to an unknown extent by a reduction in existing state revenues. This is because individuals would generally spend less consuming other goods and services because more of their income would be spent on online gambling.

That is the conclusion of our presentation, and I'd be happy to take any questions that you may have.

SENATOR WRIGHT: What I'd like to do, Members, is finish the panel. And if you'd note your questions, we will have questions of this panel at the conclusion.

So I'm going to go right to the next person on the list, and I've got my papers confused. Mr. Eadington.

PROFESSOR WILLIAM R. EADINGTON: Good morning.

SENATOR WRIGHT: Thank you, sir.

PROFESSOR EADINGTON: My name is William Eadington. I'm a professor of Economics and the director of the Institute for the Study of Gambling and Commercial Gaming at the University of Nevada, Reno.

I would like to talk today about some of the economic realities that confront Internet gambling in general and Internet poker as is being considered within the state of California. I want to address some of the pros and cons of legalization and then make some suggestions with regard to legal and regulatory structures, should the state decide to move forward on this initiative.

As Mr. Soderborg pointed out, there are certainly very important legal questions regarding compatibility of federal law, exclusivity issues dealing with tribal compacts, and the potential for exclusion of out-of-state players that will have to be addressed. This is not going to be the thrust of my remarks. Had Mr. Rittvo been here, he would have talked about some of the financial dimensions of the global Internet gaming industry, and I expect he would have said that it's approximately a \$10 to \$15 billion industry on a global basis. And in spite of the Unlawful Internet Gaming [sic] Enforcement Act of 2006, roughly half of the market is still within the United States, so it is not an insignificant industry in spite of its somewhat clouded legal status.

The arguments in favor of passage of such legislation are in the following vein:

First, one has to know that there are indeed a large number of Californians who already play because, even though the Unlawful Internet Gaming [sic] Enforcement Act of 2006 made it illegal to be a vendor of Internet gaming services or a facilitator of financial transactions of such services, it did not make it illegal to be a player, and so a lot of players still can participate without breaking the law. And there are enough loopholes in the law and ways of circumventing some of the intentions of the Unlawful Internet Gaming [sic] Enforcement Act that getting into the game is more difficult than it would be, had that act not been present but certainly not insurmountable.

Legalization has an effect that we can see by looking at other forms of legalization. Experience with other segments of gaming indicate, that if you legalize, and especially if you make a legal alternative attractive to potential consumers, this grows the market typically by a substantial factor of what prevailed under an illegal environment. So I would expect we would see something quite similar with legalization of intrastate Internet poker in California.

What we find in looking at available statistics on participation in Internet gaming in general, penetration rates are still quite low compared to other forms of gambling. But there are signs that legalization has the effect of expanding the market somewhat significantly. For example, in the United Kingdom, as of 2006, one year after the passage of the Gaming Act of 2005 that legalized Internet gaming in that country, roughly 7.2 percent of the adult population participated in Internet gaming. Three years later, that had climbed by nearly 40 percent to about 9.9 percent of the adult population. And in the United Kingdom, they have not only Internet gaming but also gaming available over mobile telephones, television, and other PDA types of devices.

One of the primary reasons for legalization—and this is true of a variety forms of gambling—is the freedom of choice and a respect for consumers to be allowed to make decisions as to how they spend their own money. This is often an issue that is not discussed in forums that are considering legalization of a variety of forms of gambling. If gambling is legal, it can be considerably more attractive than illegal or grey-area alternatives, and it also provides the potential for providing much more significant safeguards to consumers, both in perception and reality.

There is potential for tax revenue by legalization of Internet poker in the state of California, but I have to caution that tax revenue generation for Internet gaming in general is going to be limited due to the global nature of the market, especially the supplier markets for Internet gaming services. What we have seen in other countries, as they have legalized and have attempted to extract significant tax revenues, is that other jurisdictions are willing to offer

venues for service providers that have lower tax rates and less stringent regulatory environments. And, thus, we see a bit of a race to the bottom among jurisdictions competing for Internet gaming vendors.

The United Kingdom is perhaps the best example of this where they have a very substantial and reasonable law governing Internet gaming. About the same time, they still see a number of UK-based companies going abroad to the Channel Islands, to Gibraltar, to Malta, to establish themselves and lower tax and less stringent regulatory environment service, the UK market. That kind of information, I think, would be critical for the state if it decides to move forward.

That said, I think a lot of players have demonstrated a significant preference for legal forms of gaming over either illegal or grey-area forms of gambling, and I expect this would certainly be the case if California were to authorize and legalize Internet poker. Furthermore, another dimension of the industry that is important to keep in mind is, there's a tendency for a winner-take-all mentality to dominate the market, which means, that firms that become visible because of network effects and economies of scale may indeed become dominant, and this has already occurred in some of the Internet gaming companies that have emerged over the past decade. This does provide an environment where legalization within the state of California may indeed be successful, at least in certain dimensions, because of those characteristics.

Among the arguments against legalization of Internet poker in California, perhaps the most important one is that such legalization would substantially span the geographic presence of available gaming within the state. Almost all forms of permitted gambling within the state of California are venue specific, whether they are located at casinos, at racetracks, at bingo parlors, or card rooms. And even Lottery sales take place at venue-specific locations at retail outlets. If you were to legalize Internet gaming, you certainly would make it far more ubiquitous so it could take place in anyone's home and indeed in anyone's pocket off of remote gaming devices, such as iPhones. However—and this is, again, an important qualifier—there is no strong evidence that this

expansion of presence would increase the rate of problem or pathological gambling.

In the United Kingdom, for example, where they have had substantial expansion not only of remote gaming opportunities over the past decade but also a substantial expansion of convenience gaming in the form of fixed-odds betting terminals, primarily in betting shops throughout the country, the rate of incidents of pathological gambling within the UK between 1999 and 2007 remained unchanged, according to extensive surveys that were undertaken in that country. And so the evidence on the relationship between the presence of gambling and the prevalence of problem and pathological gambling is still not settled. That notwithstanding, there still is reason for legitimate concern about the problem gambling issue, especially among certain subcategories of the population, such as young males, who do tend to be the group most attracted to this kind of delivery system and, for that matter, this kind of gambling game.

One of the questions that is undoubtedly going to come up is competition with other forms of legal and permitted gambling: Would the presence of Internet poker within California cannibalize or substantially erode revenues that otherwise would accrue to lottery, to existing legal casinos? And I would point that the evidence from other jurisdictions on this is also unclear. If anything, it's suggesting that this kind of expansion may indeed grow markets by introducing more people to gaming products and gaming activities. But from a public policy perspective, I would also note that there is a question of the relevance of public policy interference. If, for example, Internet poker does not have different unintended, negative social consequences than other forms of gambling, it is not the appropriate role of policymakers to prohibit or severely constrain such activities solely to protect the economic interests of potential competitors.

However, one final point regarding arguments against gambling is, in your considerations, you have to keep in mind that legalization of Internet poker is not going to be driven by the same economic motives that lead to legalization of other forms of legal gambling. I had mentioned earlier the tax

revenue potential from Internet poker may indeed be somewhat limited. I would also note, that if we were to compare, for example, to legalization of casinos, development of casinos typically generates hundreds of millions of dollars of capital investment, job creation per facility, and the hundreds or sometimes the thousands; and therefore, many of the reasons for such legalization are the external economic spin-offs that may occur through job creation, capital investment, or tax revenue generation. With Internet gaming, we're not going to have any of these in significant dimensions. So the ultimate justification for Internet gambling or Internet poker has to be the value that accrues to potential consumers from participating in the game. There is not likely to be that much left over for the state in light of the competitive nature of the environment.

Finally, suppose the state decides to legalize Internet poker within the state of California? What kind of a regulatory structure would I recommend? I would start off by noting, I think it is the kind of activity that would lend itself best to a limited number of licenses, perhaps no more than three within the state of California. These would be licenses that could be put up for competitive bidding in a transparent and objective bidding process that parallels some of the bidding processes that have occurred with exclusive franchise casinos in different jurisdictions throughout the world. I would suggest, for example, looking at the processes used in the city state of Singapore or, more recently, in the state of Kansas.

I think it is appropriate under such a bidding process that the state delineate certain minimum requirements for participation. Potential bidders need to be fit and proper persons in terms of their backgrounds, in terms of integrity, and experience. Other minimum financial standards demonstrating any competence and capability to provide such services and to finance such services would also be a minimum requirement. It is an area that I think calls for a public/private partnership where the state does not necessarily retain ownership of the operation, but certainly it retains ownership of the right to grant a license for a specified period of time and then potential bidders can

evaluate the economic value of the proposition and in that way compete against one another and allow the state to capture a portion of the economic grants that otherwise might evolve.

I would argue against permitting credit in Internet gaming or Internet poker, and this is a challenging issue that I think would require careful analysis on the part of bill drafters and analysts. Prior deposit standards or well-defined money transfer processes should be a requirement. But, again, one must always keep in mind the potential competition with the existing Internet gaming sites and not move too far away from the offering that they give to potential customers.

I would also encourage the state to consider state-of-the-art protections against issues related to problem and pathological gambling, and many of these have been well fleshed out in other sectors of the legal gaming industries and various jurisdictions throughout the world. Issues such as self-banning or involuntary exclusion, the exclusion of minors from playing, is obviously critical and required by federal law, and one would need to use technologies in such a manner that would make it very difficult, if not impossible, for one player to play off of the account of another player.

Finally, I think the state needs to be very sensitive to the tax rates or other levies that it places upon either players directly or the vendors of such Internet gaming services because it will be important for the state to establish an environment where Internet gaming providers would be able to compete effectively against those alternatives. In my opinion, I think players would prefer to play with a legal company or entity that was established within the state of California perhaps because the comfort level that they may have and the protections that can be provided. However, too high of tax rates or too high of levies on the providers may make it very difficult for them to compete effectively in this very price-sensitive environment, and those are the extent of my comments. Thank you.

SENATOR WRIGHT: Thank you.

And, again, we're going to go back to the panel members for questions. I'm going to keep moving.

Mr. Millar, Sanford Millar, the certified specialist in taxation law, general counsel for Centaurus Games, LLC.

MR. SANFORD I. MILLAR: Thank you. And I'm also appearing this morning as a consultant to the California Travel Business Alliance. Is my microphone on?

SENATOR WRIGHT: I think so.

MR. MILLAR: Okay. Thank you.

The issues that I'm going to talk about this morning are the following: Should California legalize Internet poker? The choices are adopting, enabling legislation under the intrastate exemption of the Unlawful Gambling Enforcement Act, UIGEA, or wait for federal enabling legislation, like that being considered in the House and Senate, and then either opt out or opt in.

If the state chooses to legalize Internet poker, which regulatory model should it choose to use? The alternatives are either the monopoly model or the licensing model.

Assuming that the state acts under the intrastate exemption of the UIGEA, are the revenue and market forecasts you have seen reliable; and if not, why not? What is the effect on the forecasts of competition from offshore operators who have extraterritorial licenses? Can the state effectively limit competition from offshore operators by restricting access to sites or restricting advertising? And what competitive forces come into play? And then, finally, would the licensing of intrastate poker violate the exclusivity clauses of the tribal-state compacts? Some of the last point has been raised by other members, so I will just touch on that briefly today.

In essence, the discussion today for the foreseeable future—and for the foreseeable future—will hinge on first whether there's a viable revenue model to move the state toward regulation on an intrastate basis. And if so, what is that model—monopoly or license—and, second, what is the effect on the tribal compact exclusivity clauses?

The integrity of any revenue model is dependent on the discount attributable to the effects of offshore competition. Under a monopoly model, it's my opinion that the discount will be greater than with a licensing model. However, neither model will overcome the loss of revenue to the state if the licensing is found to violate the exclusivity clause. That's been addressed by the legislative analyst already.

A bit of background on Internet gaming. Poker is but one aspect of the Internet gaming sector. Some of the written discussion that you've received is broadly referred to all Internet gambling in describing the marketplace. We need to focus only on poker. Internet poker players break out into three discreet groups—there are individuals who play for fun only, those who play on subscription sites or virtual prize sites for fun and prizes, and those who play in real-money games. It is the real-money game group that is the focus of the regulatory effort on many scales and a source of potential licensing and income tax revenue. As a point of reference, according to the website, PokerScout.com, there are currently 13 sites that they follow that accept U.S. players for real-money poker, and all of these would appear to be accepting players from California.

There are approximately 76 jurisdictions that license Internet gambling, all forms of Internet gambling, including sports, horseracing, skill games, poker, bingo, and lotteries. There are various regulatory models that are used at the nation state level. A good example of different approaches is seen in Europe where at least two approaches are used.

One is the licensing model, and one is the monopoly model. All other models derive from these too. Both of these models have their limitations and benefits. In the United States, we have a potential third-nation state model. The U.S. model, as seen in the Frank and Menendez bills, offered in Congress in the Senate, would be a hybrid of the licensing model at the federal level, but then the states which choose to opt out can decide which model to use if they elect to regulate under the intrastate exemption.

There's also a derivative of the licensing model, and that is, the extraterritorial license which is the form of license used by offshore operators. Under this form of regulation, companies obtain licenses to operate from the licensing jurisdiction but not from within the—not in the jurisdiction. The servers and other facilities are based in the jurisdiction but the customers are not. The compliance controls, both gaming and financial, are done in accordance with regulations established by the hosting jurisdiction's licensing authority. These are typically low-tax or low-fee jurisdictions and generally allow the site operator great flexibility. Some of these jurisdictions have developed sophisticated systems and are very diligent in their supervision, but it is the extraterritorial model itself that is the foundation for the offshore operators.

The UIGEA is but one of the responses of the United States to the extraterritorial model and to the offshore operators. UIGEA, as stated somewhat earlier, provides for a ban on unlawful Internet gambling by seeking to control the flow of funds, specifically through credit cards. It is the focus of this regulation—the focus of that regulation—is on payment processors. MasterCard International, Visa International, and other credit card companies have stopped processing credit card payments originating from the United States which use the merchant code attributable to gambling, Merchant Code 7995.

It is important to note that the UIGEA regulations exempt from the processing ban—debit card systems, check collection systems, and wire systems. It is through these devices—debit cards, checks, and wires, as well as eWallet companies—that offshore companies, which have identified on PokerScout.com, are able to get money from players in the United States, including California, and then to pay out winnings.

It is only recently that the federal government has taken enforcement action against some payment processors by seizing funds on deposit and the associated records and initiated prosecutions. However, in spite of the seizures and prosecutions, the offshore operators continue to operate and grow. They

pose a serious, competitive threat to a wholly intrastate market, such as that, which California would offer.

A good point of reference to see the effect of offshore competition on a state monopoly is to look at the Swedish model. Sweden has a state-licensed monopoly system and yet it has, according to Deutsche Bank, only a 30 percent market share. The remaining 70 percent of the market share leaks to unlicensed sites operating in Sweden—operating through Sweden. The explanation is not as a result of the weakness in the Swedish regulatory system. It's an example of how the extraterritorial model works. The licensing jurisdiction allows an operator to host its operations in the licensor's facilities and reach outside its borders for customers. Sweden is a bit late in getting to the market, having entered when offshore sites have already built brand identity, similar to what would happen in California.

There are forecasts that anticipate growth in Sweden of the market share for its monopoly based upon credibility that a state license market would have, but the competitive forces will still be there. It should also be noted that Lotto-Quebec announced on February 6, that as the monopoly online operator in Quebec Province, it will, offer online poker in the second half of this year. But Italy, also a prior monopoly model, has moved to a licensing model. It is worth noting that there is no homogenous license fee, or tax rate, through the various licensing jurisdictions that license Internet poker or Internet gambling.

Examples of the current tax rate differentials are found in the Italian approach. In the Italian regulatory regime, there is a differentiated tax license rate. The rates vary from 20 percent of revenue for cash games and for casino games to 3 percent for poker. Other examples of licensing jurisdictions are Gibraltar which has an annual license fee of 1 percent and the U.K. which has a licensing fee, which is based on 15 percent of gross profits.

What is important to note is that the economic risk in the two models is very different. In the state monopoly jurisdiction, the operator typically pays a fee to the software and technology operator and the state bears most of the market risk, including the risk from offshore competition. The risk of success

is shifted to or borne by the state. In the licensing model, the licensee has the entrepreneurial risk. The Swedish experience is an example of what happens when a monopoly model is faced with offshore competition. The Italians are also illustrative for having moved from a monopoly to a licensing model. But these, again, are nation state jurisdictions.

The unknown factor here is consumer behavior. How will consumers respond when faced with a choice of a regulated, wholly instate activity, which requires proper identification, tax compliance, age, and location monitoring when there will still be access to offshore operators?

There are several methods of attempting to control consumer behavior by regulating the Internet, none of which truly successfully impair the extraterritorial reach of unlicensed companies. The methods breakdown into, (1) nation-state censorship, (2) advertising bans by imposing sanctions on Internet service providers, and (3) censorship of other forms of media advertising. None of these approaches, in and of themselves, work on a nation-state imposed basis, let alone have they been proven to work in what would be an intrastate or single-state example. There is a fourth approach, however, in trying to drive compliance, and that is, through the tax-compliance efforts, which have barely been discussed in the course of the processes up to this point today.

But here are some of the methods used to avoid censorship by the extraterritorial operators and to attract new customers. First, the operators have free play sites that sponsor television programs. These sites use a domain URL that usually ends in .net or .tv. The consumer is counted on to recognize that the most common domain is .com. The consumer may instinctively direct himself or herself to the .com site. In addition, these sites use online magazines and information sites to host advertising for their .com site. They also use blogs and use traditional print. The operators use these in combinations with customer signup bonuses and retention bonuses and celebrity endorsements, all of which serve to build their brands and their market share.

It is worth noting, that on most of the prominent offshore sites, a full 75 to 80 percent of all players are playing for free. The play-for-free offer and learn to play is a key recruiting tool for real-money games. Further and most importantly, the extraterritorial operators are not limited by geography. They create player liquidity pools on a global basis as opposed to having to deal with a physically restricted geography and inelastic pool of players. The global reach allows for constant regeneration of players. The question then before you is, Can the state license operating site operate in a fixed geographic boundary and compete for market share with already established, well-branded offshore operators? Put differently, Is censorship an answer? The answer is, no.

Internet censorship is a highly controversial issue and one that should be considered, with all do caution, and in light of already existing abilities to avoid restrictions on marketing by nation state regulators, it is doubtful that California could implement a system of Internet advertising censorship that would pass legal challenge and work. This committee should recognize that any proposal that bases its license fee forecast to the state on a premise of Internet censorship is deeply flawed. Further, Internet service provider regulation, while tried in Italy, has not proved to be truly effective when done at the nation state level. It is doubtful whether the state could impose ISP blocking that did not meet federal challenges.

In essence, the intrastate model may very well ring fence California by preventing it from reaching players outside the border of the state but yet be a target for offshore operators who choose to continue or choose to enter this market. They can add—they, they offshore operators—can add to their player liquidity pool by drawing from California, but California could not reach outside its borders.

As I stated to you earlier, I consulted with Michael Genest on the letter delivered to the CTBA which you should all have. I did so with the understanding that I would testify here today with the expressed purpose of helping you to find a path through the conflicting opinions and proposals. The market revenue data is difficult to assess because most of the analysis is based

upon projections of what will happen using assumptions that may not accurately assess the effects of offshore site competition. The just-mentioned issues should be sufficient to cause concern about any revenue forecast that does not consider the effect of offshore competition.

But in the Genest letter, we discussed the fiscal repercussions of violating the exclusivity clause. We've already discussed the revenue impact, but one of the key points that is not discussed in any of the forecasts, Members of the Committee, is that the compact revenue has an estimated life of 20 years which must be balanced against the uncertain forecast of consumer behavior on an Internet poker site with a geographically defined player pool.

It has been stated by some compact members that licensing of Internet poker would violate the exclusivity clause of the amendments of 2004 and '06. The important point here is not whether that occurs or doesn't occur, but there is no 20-year Net Present Value forecast by any proponent that forecasts Internet poker revenue from a wholly intrastate operation in California. This is an important omission from the data as the NPV of the two income streams needs to be compared, not just for the short-term periods but in order to determine the real cost benefit of regulation on an intrastate basis. I realize that there may be differences of opinion on the intrastate exemption, and I defer to others who are perhaps more skilled or more fluent in that issue who may be appearing later today.

There are some who suggest that the state wait and see if the proposal is being discussed in the House and Senate produce a federal bill and then make a decision on whether to opt in or opt out. There are others who suggest that the state move now and move forward on an intrastate basis. There may be some merit in deferral to gather more data and better enable the state to make an informed decision on whether to join a federal regime or not and which model—monopoly or licensing—to choose, should the state so decide.

I would offer a comment, in addition to those in my prepared remarks, that my personal preference is a licensing model and the marketplace should be the decider as to who bids and who doesn't bid rather than the state limiting

the licensing to a particular mechanism itself. And with that, I'd like to conclude my remarks. Thank you.

SENATOR WRIGHT: Thank you very much.

We're going to keep moving again. Members who just came, we're going to save all the questions for this panel until the end, and there probably will be some questions.

Mr. Catania, the president of Catania Consulting Group.

MR. FRANK CATANIA: Catania. Thank you, Mr. Chairman.

SENATOR WRIGHT: Excuse me. I'm going to learn English after a while too so I apologize.

MR. CATANIA: Members of the Committee, by way of introduction, I'm a former deputy speaker of the New Jersey General Assembly, former assistant attorney general, and director of the Division of Gaming Enforcement in New Jersey. Currently I am a partner in the Catania Gaming Consultants and the Law firm of Catania & Ehrlich. I have been interested in the Internet gambling since the mid-1990s when I was directed Division of Gaming Enforcement. My businesses have assisted provinces, foreign governments, and private companies in establishing strict regulations for the oversight of Internet poker and other forms of Internet gambling.

My position for intrastate Internet poker regulation is actually concentrated on the identical issues raised by opponents of Internet gambling. If I could make only one suggestion to California in considering regulating intrastate Internet poker, it would be to get regulations right from the start. I am also concerned about underage and problem gamblings. But since Internet gambling is already here and attempts at prohibition have not worked, a better solution lies in a strictly regulated alternative aimed at ensuring the presence of harm minimization measures.

Just as with traditional casinos, there are four key elements of effective Internet poker regulation. First, you must ensure the integrity and financial resources of the operators; second, you must ensure that the games are fair; third, you must provide player protections, including procedures to exclude

minors and assist problem gamblers; finally, you must have provisions to prevent money laundering and other criminal activity.

Starting with the prospective operators, it is essential that they be investigated to determine their good character, honesty, and integrity. They must also have gaming experience to operate an online poker site and the financial resources to guarantee that winners will be paid. These background investigations should include those who own or control the operating company as well as key employees. The same qualifications required of operators and key personnel should also apply to those who own or control the suppliers of software platforms used by the various licensed operators. Their key personnel should also have background checks. Since online gaming payment processors are an important part of the online gaming operation, they too should comply with the same standards set for the operators and the software providers.

Online poker relies on the existence of reliable software, without which an online poker site could not exist. Regulators must be convinced that the software being used by the operators is fair and honest. The online poker site must be shown to operate with complete randomness so that each player has exactly the same chance of winning. To do this type of testing, experts are needed. The testing facility must have the experience to understand the online poker site's operating system and the potential for fraudulent activity by the patrons or the operator. To do this, the software being used must be tested by an accredited testing facility with experience in testing server-based games. Testing is what will assure the fairness of the games being offered.

Game servers and backup servers that record all play must be kept in a safe and secure location, accessible by only authorized personnel and agents of a regulatory agency. This is essential to prevent anyone from tampering with the software. Backup logs must be kept by all operators. These logs provide a picture of all aspects of play and must be kept for a prescribed time period set by regulations. This is so important that regulations should include provisions that a failure to keep backup logs as required would be cause for a license suspension or revocation.

The regulators' responsibility cannot end with the pre-testing of the random number generator in the source code. Just as in land-based gambling, monitoring must be continuous. Outcome-based monitoring by internal auditors should also be required. This type monitoring is conducted to prove that games already conducted have been fair and honest and the operator has complied with all regulatory requirements. This internal audit, as well as an external audit, should be presented to the regulators periodically to assure that there has not been any cheating by the players or, again, the licensee.

e-Commerce Online Gaming Regulation and Assurance, eCOGRA for short, is a regulatory group based in London that has created generally accepted procedures for all types of online gambling and a model for online gambling regulation. The eCOGRA standards essentially constitute a collection of global best practices. eCOGRA requires their licensees to comply with certain procedures, and an independent auditing team reviews their licensees' compliance yearly. Failure to comply with the eCOGRA seal—failure to comply with the eCOGRA seal—could result in the seal being removed from the licensee's website.

Since Internet poker would be offered to participants located only within the state of California, operators must be compliant with software that is able to determine the exact location of the player. This is absolutely essential, since expansion beyond the state of California would raise issues about legality under federal law. Software of this type is available and has been successfully employed by online gaming operators located in licensed jurisdictions around the world to exclude players from the United States or other jurisdictions where the legality of Internet gaming is questionable. This does not mean that there will never be an incident where a player outside of California gets through the register. No system is 100 percent. Even in land-based casinos, there is an occasional underage player that gets past security.

In this regard, a safe and secure manner in which a player registered to play is a necessity. The operator must verify the player's identity, age, and location. Software to do this currently is available and has been tested and

used by existing online poker operators for several years. Licensees must make it a priority to know their players, to also avoid the possibility of money laundering and other illegal activities.

A very important part of the regulatory structure is player protections. A link to problem gambling sites should be easily visible on each site. Players should be allowed to set time or loss limits for play. Players should be also provided the ability to self-exclude from play. If a player bars himself, him or herself, no site regulated in California should allow that player to play until that player follows set procedures according to regulations to remove him or herself from the exclusion list.

My experience in both land-based and Internet gaming tells me that Internet poker can be better regulated than casino gaming. In disputes or investigations in land-based casinos and poker rooms, operators and regulators rely on video from closed-circuit TV. This method of investigation is dependent on the camera working and being focused on the right spot at the right time. Internet poker, on the other hand, has real-time auditing, which means the system can provide the operator or the regulator with records instantly or from a previous period.

To conclude, the state of California has the experience to regulate gaming through the Bureau of Gambling Control. With regard to online gambling, with regard to online poker, the responsibility to regulate intrastate Internet poker should be assigned to the Bureau which must be given the resources to regulate online poker properly. The Bureau is familiar with and has been doing background investigations, such as the ones required for online poker.

Additionally, staff with the technical knowledge regarding the workings of the Internet will likely also be needed, but the cost of any additional staff can be transferred to the licensees, as is the practice in many land-based gaming jurisdictions. It is essential to have staff or third-party agencies that have the ability and knowledge to understand the online operations of the licensees.

Although I focused on the benefits of a well-regulated intrastate Internet poker to the player, I should also touch on the potential economic benefits to

California. As my firm has previously advised governments in other jurisdictions, a well-regulated online gaming industry results in private investment in the technology sector and creates many high-skilled, high-paying jobs. Regulation also generates many potential levels of taxation—business, gaming, payroll, et cetera—which can be used to fund social programs, particularly those related to gaming. Of course, these benefits are maximized where the government adopts an open, regulated free market, allowing multiple licensed operators.

Mr. Chairman, thank you.

SENATOR WRIGHT: Thank you, Assemblyman. We'll still let you keep the title, and you might get jumped on in the hall but that's okay. We won't sweat you about that.

The final person on this panel, Chris Derossi—did I pronounce that correctly?

MR. CHRIS DEROSS: It's Derossi.

SENATOR WRIGHT: Derossi. Okay.

MR. DEROSS: Thank you, Mr. Chairman.

SENATOR WRIGHT: I was going to get it wrong either way. I had a 50/50 chance. The CEO and chief architect of CyberArts, welcome. Go ahead, sir.

MR. DEROSS: Thank you, Mr. Chairman and Members.

My remarks are primarily directed toward the technology capabilities available today and the best practices that would enable the implementation of some of the requirements that were just outlined by Mr. Catania and Professor Eadington earlier in the testimony.

Internet poker technology has been around for about 12 years now. The first online Internet poker site went live in January of 1988. So we've had a little more than a dozen years now for the technology to mature, find its weaknesses, and get them corrected.

There have been a few milestones which have acted as prods to specific technology advances in this regard. In 2003, television programs started

heavily promoting poker. It's when it largely captured the American attention, and the advertising for online poker sites created a surge in awareness and demand which at the time caused much of the technology to fail. But in response, it also caused the technology development to become more robust, more stable, and more scalable for large volumes of players such as might be seen in the population that would participate within the state of California.

Of course, in 2006, when the UIGEA Act was passed, many of the companies that were formerly targeting the United States voluntarily opted out of that participation, dropping their player base by up to 50 percent in many cases. This actually created a little bit of breathing room from a technology perspective, allowing the technology more time to stabilize and mature as the markets started to evolve and shift. And I will also mention the incident in January 2008 where a cheating scandal was exposed that had been going on for multiple years where people associated with the technology providers and the operators had been cheating the players by using backdoor capabilities in the software leading to an awareness of the requirements, as Mr. Catania said, for source-code audits and independent verification by third-party organizations.

So the trends and technology today mimic those that would be required for a California intrastate poker offering. We are seeing, as has been mentioned on the panel, other ring-fenced operations, particularly in places like Sweden and Italy. This is also associated with the regulatory body's desire to implement stronger player protections, consumer awareness, and responsible gaming. So those emphases have translated into changes to the technology itself.

I'll talk for a moment about the capability of technology to actually ensure that players are within the geography that is defined. The state of California specifically in this case, there is software to do this. There are multiple service providers that have been doing this at both country, state, and even local municipality levels. The accuracy at this point is very, very high and is constantly being refined. A simple accuracy for locating a player with each

and every wager placed with each and every connection is greater than 96 percent to identify somebody as being within the state of California or not. That could possibly be increased through further technological advancements, depending on what the requirements might be.

The ability to identify your customer and validate their age is also quite possible today. There are again services operating, catering to other gaming jurisdictions around the world which are specifically designed to make sure that players are who they claim to be, that they are a resident where they claim their address is, and that they are the age that they say they are. This works by taking things like credit bureau reporting data, the same people that collect your credit histories, and validating the birth date that you enter. So if you enter a birth date and it can't be found, you're automatically excluded. If you enter a birth date and it's incorrect, you're automatically excluded. The only way you're permitted to play is if you enter a birth date that can be confirmed through these credit reporting data, and that birth date indicates that you're over the age of majority in this state. So it's a very robust system and not very well tamperable, so those capabilities do also exist.

In terms of identity verification, technological capabilities, like the ones I just mentioned, do exist and also verify things like place of address, previous residency. Those of you who may have used online banking services that check your identity based on asking questions from your own personal financial history will find that those things are very sophisticated to date, and the online gaming industry has access to the exact same technologies that the online banking systems use to date.

These are the kinds of best practices which are being put in place around the world and are operational, as we speak, in Europe today. This is not cutting edge; this is not unknown or breaking new-ground territory. These are things that there is quite a bit of experience, which I hope you'll hear from some of the other speakers later today, in their use. We do know that technology is never, of course, the complete solution, and many of the procedures that are required go hand in hand with the technological solutions.

So age and identity verification, for example, isn't always a technological solution but is often simply a matter of sending in copies of your driver's license, passport, or other identification, and being checked by humans on a regular basis. So there's always a human oversight that increases the accuracy.

And then probably one of the largest areas of technological focus at the moment is consumer protection and responsible gaming. There are many, many ways to ensure responsible gaming in online poker today. They are—some of them have already been mentioned—the ability for customers to self-exclude and blocked from play online, deposit limits; there are jurisdictions with legislation that requires automatic withdrawal after your bank account, if you've won a large amount, after your account reaches a certain threshold, it is automatically withdrawn and taken out of the gaming system to discourage you from simply losing back everything that you've just won. Lost limits and daily wager maximums are common and available in the technology today, as are various time limits, time warnings, and even enforced breaks by the software, something that you can't possibly get in an online casino or an offline brick-and-mortar casino but definitely possible online.

Even more sophisticated than that are things like player behavior-trend analysis—the ability to identify a player's behavior or a change in their behavior that indicates they may be entering into an irresponsible gaming cycle, going on tilt, as they say in the poker world. It is possible to detect that earlier in software than it is in a brick-and-mortar world and far more than just placing a link to responsible gaming sites or gamblers' awareness sites. The software can take active measures to reduce a player's access to the higher-stakes games or to even enforce breaks or temporary exclusions. It's already been mentioned that the industry has a self-regulating body, the ecogra.org, responsible gaming initiative, and this has been around for a while.

And then finally in terms of various consumer protections, some of the concerns that exist in the Internet poker world focus around cheating and collusion by other players. This is always going to happen, of course. It's an

imperfect world full of humans and people will always try. The good news is, that unlike a brick-and-mortar world, you have the data for every single deposit, every single withdraw, every single card dealt, wager made, game one, and every action by every single player. This is far more information than you're ever going to get in a physical card room or casino, and it does allow you to monitor for potential cheating behavior and cheating activity in real time in ways that is otherwise not possible in the offline world.

Human judgment is essential. There's no way to get around humans evaluating player behavior, but it can be greatly assisted by the technology today. Technology, for example, in online poker can flag incidences of questionable behavior, doing things which would not otherwise be rational behavior in a poker game, but might be done in order to facilitate cheating, can be detected by the software and alert an operator literally in real time so that that incident can be checked before the player leaves the virtual table. Those kinds of protections are definitely possible and serve as a benefit in the online world over and above the offline world.

And then finally, just to touch on it, I've said this previously, but the security of the online banking technology is the same technology used for the online poker. So those consumers who trust their online banks should have no difficulty trusting the online poker world, and regulations should ensure that that level of security is required at a minimum. And with that, most of my other comments have been addressed so I'll conclude then.

SENATOR WRIGHT: That concludes this panel. Any questions from the members?

Senator Harman.

SENATOR HARMAN: Thank you, Mr. Chairman, I had a question for Mr. Eadington.

In your testimony and in your written comments, you indicated that "there are presently a large number of Californians who participate in Internet poker." Has that number ever been quantified? Do we know how many are

currently playing Internet poker and have there been any studies, or what do we base that on?

PROFESSOR EADINGTON: My knowledge on that is really third party or anecdotal. Regrettably, Mr. Rittvo, who was supposed to be here, I think, would have had much more to say on that issue. Based on studies in other jurisdictions, the penetration rate of Internet gambling is in the 5 to 6 or 7 percent range. Poker, as was mentioned, is a segment of that particular marketplace. Using other jurisdictions like the U.K. as a base, one might estimate that the number of active Internet poker players in California is somewhere in the half a million range perhaps but very hard to say.

SENATOR HARMAN: So it's basically an estimate and we don't really have hard evidence. There's no way to track it, is there, of who's playing and who isn't playing? Is that a fair statement?

PROFESSOR EADINGTON: Well, there probably would be within the companies that are offering the services, of course.

SENATOR HARMAN: Sure, sure.

PROFESSOR EADINGTON: They may have that capability. And you have some companies that were public before the Unlawful Internet Gaming [sic] came into being. And from their revenue generation, you can work backwards and get some estimate as to volume of play that they were dealing with.

SENATOR HARMAN: Did you want to comment on the question?

MR. MILLAR ??: Yeah. Basically, Dr. Eadington has it pretty correctly. The estimate's based upon public source data show that California, with about 12 percent of the population, actually has about 15 percent of the nationwide play. If you look at the public source data using Poker Site Scout as a measuring run—and I'll explain why in a moment—you can look at their annual trending or their daily trending, depending upon which focus the analyst can look at, and then do an interpolation of that data to come up with an estimate as to what the revenue is on a per-hour, per-day, per-week, per-month basis. So there is a methodology upon which you could come up with

an estimate. But again, it would be an estimate and it would be limited to the following criteria: The first and foremost is that some of the estimates are disjointed by reason of the fact that a large number of the games that are measured on Scout reflect high-dollar games which are not traditionally good estimates of the number of players. They're only estimates of revenue.

Scout, as the analysts have all become familiar with, I hope, has cookies that sit inside the 13 sites it measures and tracks real play in real time. The other methodology to be used is to look at certain of the sites who have meters that show exactly how many people they estimate are actually playing on the site on a global basis. You can subtract one from the other and get the estimate as to the free players.

SENATOR HARMAN: Okay. Thank you very much.

SENATOR WRIGHT: Senator Harman, when we go to Panel VIII, the Players, there are a couple of associations in that group that will have some additional information on the locations of some of the players.

Senator Price.

SENATOR CURREN D. PRICE, JR.: Thank you, Mr. Chairman, and to the panel thus far.

As far as I can tell, that Leg Counsel has not opined yet. I wonder if you gentlemen might have some thoughts as to which class would Internet poker fall up under—Class 1, 2, or 3?

MR. MILLAR: We've expressed an opinion in our written materials that we believe the Legislative Counsel in its analysis of the 2006 Act, it did not correctly take into consideration national...

SENATOR HARMAN: I don't think your microphone is on. You might want to press—yeah, I guess it is. All right.

MR. MILLAR: Okay. We've expressed an opinion in the written materials that we submitted that we thought the Legislative Counsel's opinion that was written in April of 2008 came to an incomplete conclusion or an inaccurate conclusion that should be reconsidered and that the use of Internet poker or

the use of computers at home or anywhere else to play games constituted a Class 3 implement.

SENATOR PRICE: That's your analysis?

MR. MILLAR: Yes.

SENATOR WRIGHT: Okay. Senator Yee.

SENATOR LELAND Y. YEE: Thank you very much, Mr. Chair.

You know, let me toss this question out; and if nobody wants to pick it up, let me direct it to particular individuals. But given the fact that there's been some suggestion that if we in fact, the state of California, engages in Internet poker, that that may in fact violate some of the compacts that we have entered into with some of the Indian nations.

Do you have any comments about that particular statement? Do you feel that in fact we would be violating those compacts or not? Do you have an opinion about—do any of you have an opinion about that?

MR. MILLAR: We've expressed an opinion in writing, both in the Genest letters and in my written comments, that the exclusivity clause is at serious risk and there would be contention among them, the participants to the compacts over the enforcement of the clauses.

SENATOR YEE: Anybody else want to offer an opinion? Mr. Catania?

MR. CATANIA: I couldn't say. I would—I'm not familiar with it. I just can't answer you.

SENATOR YEE: But do you feel that the state of California can in fact establish some kind of Internet poker operation, state-sponsored Internet poker operation, within the state of California?

MR. CATANIA: I do. I don't think it should be state sponsored or monopoly by the state. I think what it should be, it should be an open market. You know, companies should be allowed to apply for licenses; licenses should be issued. And again, it should be well regulated. By doing this, you're inciting them to defer ?? competition between themselves, and they know what they're doing. I mean, right now Internet poker, you know, comes from other places, like the Isle of Man and other jurisdictions, is probably one of the

largest sectors of online gambling and does very well. And I think it would do very well here in California as well. You know, other states at the same time are looking this. I mean, it's not only California. New Jersey has some legislation which has to be a little bit different than California because there, they have a constitutional issue that, again, can only take place in Atlantic City. However, the legislation that's been introduced there says that the gaming takes place at the server which has to be located in a casino so it would not be a violation of the constitution, and they would then only offer it to intrastate.

Also, there's some rumblings about the state of Florida doing, you know, doing the same thing. So it's something that, you know, I, as I indicated, in 1996, I think it was, when I was director, and I had my staff look at Internet gambling because it was just coming on the radar, and we made a recommendation to the governor at that time that very little you can do to prohibit it. We should try to regulate it.

SENATOR WRIGHT: Okay. Any other comments? Thank you.

We'll look at a couple of questions, I think, and we had some discussion relative to, Does it grow the pool of people who play? Do we take away from the people who are already going into facilities? I know in the panel we kind of left that question up in the air in terms of, specifically, do we add more players who aren't going to play? What potential likelihood do we have to take players who are playing offshore to bring them into a California site? And this would be Californians, obviously, who are currently playing offshore to come to a California site. I mean, I throw it to the panel.

MR. CATANIA: I don't think you're going to see that much of a takeaway from the land-based casinos. I think you have different type of players. I think the player that's online is probably younger, more technologically acclimated to the Internet and, you know, is staying away from the glamour and the glitz of the casinos. I think the people that still go to casinos are still going to be going there. I think that, if anything, it's going to increase the pool.

MR. MILLAR: Mr. Chairman, I think that Mr. Catania has it right, that these are discreet markets, but they become constructive to each other, depending upon the marketing tools that are used. There are two particular—one particular—operation that runs a large land-based tournament that has used the online system to enhance its brick-and-mortar business quite effectively. Whether that kind of system could be implemented in California has to do with brand identification. It has to do with marketing experience, and it has to do with whether there are adequate tournament drivers to bring people in. But there's no evidence that we've seen that shows that this is destructive of discretionary time or destructive of discretionary money when used on the Internet. I think they are discreet markets, except for that conjunction that I just described.

PROFESSOR EADINGTON: I would point out there have been a number of academic studies that have looked at crossover-demand issues between, for example, lottery and casinos or racing and lottery casinos. And for the most part, they do find these as discreet markets that do not take strongly of weighing one from the other. The psychology of a poker player is quite different than the psychology of a slot machine player, for example, and I think the demographic of an Internet poker player is going to be much younger, predominantly male, and I suggest, as we have seen in retail, a lot of organizations who had brick-and-mortar operations would look at Internet gaming as a potential feeder market and a way of growing the customer base for the next generation.

So I think the arguments about cannibalization are probably far less important than the arguments about expanding the pool of actual gamblers in a variety of delivery systems.

MR. SODERBORG: The only thing I wanted to note is, that when we made the point that it may redirect revenue from other sources in the economy, we weren't restricting our analysis only to gambling. We meant, in general, people would have to spend, take money that they would have spent somewhere, whether that's just general consumption, groceries, or other forms

of entertainment, and would direct it to the website, and that might generate somewhat of a revenue offset for the state.

SENATOR WRIGHT: I was going to say as well, Mr. Millar, when you were referencing Sweden, we actually have some folk from Sweden here. What we might end up is what they've got, is 30 percent of their market, but they were similar to California and, that before that, they were getting 100 percent of nothing. So 30 percent of something is better than 100 percent of nothing which is currently what California gets.

MR. MILLAR: Well, I think the argument that I was making, sir, Mr. Chairman, was not...

SENATOR WRIGHT: _____.

MR. MILLAR: Okay. The argument or the position that I was putting forth was that, in an already matured market where there were customers that have brand loyalties established, entering as a state monopoly has its problems. Now grabbing 30 percent market share is not a trivial market-share aspiration, and there are some forecasts that indicate that their market share may grow beyond 30 percent in the near future, depending upon a variety of marketing tactics and methodologies deployed.

What I did point out, though, is, or would like to assert is, that the possibility for that market share as a state-revenue model as opposed to a state-actor model are different. And in a licensing model, there is an incentive for people that are already branded to come into the marketplace and participate and bring their brand identification, their server technology, their personnel, and locate physically in the state and generate jobs; whereas using a state monopoly, there is no incentive for them to cooperate in their marketing efforts at all. There's no revenue share that's going to be derived. It will be a much harder, competitive market if you go to a monopoly market as opposed to a licensing market, assume you get past all other issues.

SENATOR WRIGHT: And we're probably saying the same thing in a different way. We're a long way from figuring whether or not we're going to have the licensing from a monopoly model. But, again, as you indicated, I

would suggest, that if they started at roughly 30 percent and, as I understand from the folk from Sweden that we'll hear from later, that their market share is growing. And considering that they started from zero, that, you know—again in the South, we have an expression that goes, “And is better than none/nan.” ?? And since they weren't getting anything before, then 30 percent is not a bad slice to take. But to your point, the methodology that we use between monopoly and licensing and all the other things that we have to take into account would certainly determine what we do. And I'm not to say that you suggested that the 30 percent is trivial, but it kind of was a, wow, they only got 30 percent but they started from zero.

MR. MILLAR: Could I respond on one...

SENATOR WRIGHT: Please.

MR. MILLAR: ...additional point, Mr. Chairman, and that is, the following: What we've all been focusing on is the regulation by way of gaming regulation or technology regulation. What we haven't focused on is the leaching of revenue that's currently occurring. And that's a separate focus that I think should not be overlooked, which is, there is revenue income taxes that conceivably are missing from California residents who are playing online, companies based upon long-arm jurisdiction that should be the subject of enforcement proceedings, and those are separate and discreet issues which is, Can we capture currently leaching revenue as opposed to going to another regulatory regime to do exactly the same thing that we're not currently doing? Now if there is mechanism within a revenue and taxation code or other sections of California law to do that, it may be worthwhile looking at it to see if in fact through information exchange agreements with the Internal Revenue Service information can be obtained that would allow for proper enforcement actions to occur.

SENATOR WRIGHT: Okay. And one other question. I mean, I think, to the issue of the exclusivity, we will probably go around that and it will probably be resolved in court. I mean, the question as to a gaming device, we've never really pushed that. And the time that it got close, it wasn't resolved because

we simply outlawed the device. So the issue from a regulatory standpoint has never been clear. So does it happen—I don't know. That means we'll probably end up in court on that issue.

Certainly, if it's determined that it does, then that would change the model because now, rather than looking at how much revenue you get starting from zero, you would have to subtract out the revenue or that portion that you would lose which would certainly change the metric and how you had to look at it. But it wouldn't change the dynamic that there is currently a river of cash that's leaving California for which we currently get absolutely nothing.

MR. MILLAR: Well, I would suggest, based upon what we just discussed, that the Revenue and Taxation Code and the Internal Revenue Code can be used effectively to at least look at work as a stopgap to pick up some of that leaching revenue while these other issues are worked out, either on a political or judicial basis.

SENATOR WRIGHT: Right. And that might be, you know, where we end up. But, you know, if we were in the game, again, even if we took the Swedish model, if we got 30 percent of X and pursued the other methods with respect to the Rev and Tax Code and the other things as possible, I mean, there might be an opportunity for additional revenue as well. So, I mean, there's no reason that you limit yourself to one or the other. It might be that you do the Rev and Tax Code, see what cooperation you can get from the IRS. I suspect the IRS is also missing a lot of cash in this exchange as well, so they too may have the interest in participating with states like California, if that could be captured, as well as looking at pursuing our own angle, notwithstanding what Judge Wapner would say relative to whether or not this violates the issue of the gaming device.

But let me—Senator Yee, you had another question.

SENATOR YEE: Thank you very much, Mr. Chair.

I have two follow-up. I think a couple of you had mentioned about discreet markets. And so if in fact the Internet poker is a discreet market from the slot machines, then the objection from the Indian tribes, in terms of the

state of California getting involved in Internet poker is really not about them losing market share. Is that a correct statement?

MR. MILLAR: I would defer to their positions on that, and I'm sure you're going to hear from them later. I would certainly...

SENATOR YEE: But you would agree with that statement then?

MR. MILLAR: Well, I would agree with the following...

SENATOR YEE: Because they're discreet, you know.

MR. MILLAR: Well, I said that they are somewhat integrated, depending on crossover points. I would make one other example put forward to make your life even more difficult, Senator, and that is, that using player bonus points, player recruitment points, player comp points, which is what they're called in the industry on the brick-and-mortar side, offering games where people play not only for cash games but they play for points that recruit people into their brick-and-mortar operations, is a hybrid model that some companies are looking at quite aggressively as a method of player retention and player recruitment, driving people to the buffet, driving people to rooms, driving people to other incentives. So there is a homogeneity that occurs within the marketplace or that can occur within the marketplace. So the ability to attract players as opposed to lose them also exists. So I would bring that to your attention just to consider as you hear from brick-and-mortar operators and the tribes in particular.

SENATOR YEE: Then the other point that I want to sort of explore a little bit more is this thing about, you know, that we have some leakage because of the fact that the Internet poker, you know, is not something that the state of California now regulates and so on. If we don't regulate that and if it maybe goes inside a tribal nation, then the state of California really doesn't have all of the tools within its toolbox to really know exactly how much money is being made off of Internet poker. Isn't that also the case?

MR. MILLAR: Well, I think you have a question of whether the conclusions you come to are intuitive or fact driven, and much of what you just

said is intuitive or inductive. I mean, we don't have hard data as to how much is actually leaking from California. That's correct. In part...

SENATOR YEE: You know, I think we're trying to get into this because I think we have, you know, some strong, highly probable statements or facts whereby people are playing Internet poker...

MR. MILLAR: Oh, absolutely.

SENATOR YEE: ...and their revenues are going and we have not a clue how much and where and so on, right? So that's really why we're, you know, involved in this particular discussion.

MR. MILLAR: What we have is imperfect approaches. The revenue-and-taxation approach, the tax-enforcement approach is imperfect because some of these companies are offshore. The ability to get to data is imperfect on the part of the player participation. And a regulated model, which does not effectively deal with the offshore extraterritorial license holders, is equally going to be imperfect. It may result in the 30-percent-of-something approach, but it's an imperfect model. They were all imperfect. The comments made by my co-panelist, Mr. Catania, and others about offering licenses and competitive bidding processes to try and bring in the most number of players is a reasonable conclusion to come to, subject to coming up with a political or other resolution with the exclusivity clause.

SENATOR YEE: But getting back to, I think, my original point, and that is, that, you know, if we are going to somehow be able to cobble whatever money we're losing, that the only place that we can in fact realistically and honestly and accurately cobble those dollars together, are those sites, locations where the state of California has some jurisdiction, we don't have no jurisdiction over the Indian nation.

MR. MILLAR: Oh, I understand what you're saying, Senator.

SENATOR YEE: Yeah. I mean, if we don't get involved in this, the state of California does not get involved in this, we're going to continue to lose those resources if in fact we buy into this argument that, well, we can do it but

maybe the Indians can do it. Then, you know, they're outside of our reach too. And so at the end of the day, we're still going to lose all those resources.

MR. MILLAR: I'm just going to defer to other people in the later panels who will address that issue, I think, better than I can, Senator.

MR. CATANIA: The only way that the state of California is going to receive any revenue is for them to do licensing and regulation.

SENATOR WRIGHT: I think too we should be clear that an Indian tribe involved in Internet poker becomes a business entity like any other entity. The sovereignty issues that go to an Indian tribe only apply if the gambling is taking place on the reservation. So at the point that they leave the reservation as a business entity, they become just like any other entity doing business in California. That's at least the rules here. So they would be in business like anyone else once that gambling leaves the boundaries of the reservation.

But let me thank this panel.

Mr. Derossi, if I was making a comment about, if somebody was doing something that just seemed illogical, would that be like an on-side kick at halftime? (Laughter)

MR. DEROSI: Yeah, exactly.

SENATOR WRIGHT: I hope they wouldn't, you know, throw me out of the game if I made the on-side kick at halftime or, you know, or going for it on fourth and three—but anyway, thank you all for coming.

MR. MILLAR: Thank you, Mr. Chairman.

SENATOR WRIGHT: We will move on with the first—and your information was helpful. I appreciate those of you who traveled from further away, from New Jersey and Los Angeles, which is a great town, by the way, and Reno and the LAO. Thank you all for coming.

We'll add the second panel if you guys would come forward.

I'm going to ask Simon Holliday from Great Britain if he is still here.

So, Jonas, I'm going to really mispronounce because my Swedish is just awful. But Jonas Söderlund, Robert Stocker, and Robert Holliday, if you would come forward.

For folk who don't have Mr. Holliday's background, he is the founder and CEO of H2 Gambling Capital. He is internationally known and respected as the leading financial analysis consultancy and the supplier of data regarding the gaming industry, both land and online. For the past eight years, H2 has focused solely on gambling, advising, and on supplying information data to both industry and financial sector.

Again, Gentlemen, welcome aboard, and I'm just going to start right in.

Mr. Söderlund, if you would go first and, again, thank you. You know, we have to give—I'm not quite sure what the trophy is yet, but there's got to be some award that goes to the person who traveled the furthest. I mean, my geography's bad. I'm not sure what was going to be up between Italy and Sweden. I think Sweden would probably be still a little bit further away so you still get the prize. We haven't figured out what the prize is but there's that gift that goes to the guy who traveled the furthest.

Welcome to California, sir, and thank you for lending us your information.

MR. JONAS SÖDERLUND: Thank you very much. I have prepared a statement. I have it as well if he wants to have a copy of it.

To start, I would like to start saying, I'm very glad to be invited today, Government Organization Committee of California State Senate hearing, regarding online poker. So on behalf of the Kingdom of Sweden, I want to thank you for this opportunity to describe the regulation of online poker in Sweden.

My name is Jonas Söderlund and I am the head of Business Intelligence at the Swedish Gaming Board, and my main responsibility the last three years has been to control the concession holders, that they are following current regulations...

SENATOR WRIGHT: Mr. Söderlund, I'm going to—just a second. I'm going to grab your copy there. Okay. Thank you. Go ahead.

MR. SÖDERLUND: ...in other words, compliance, and explain a little bit about the game involved in Sweden. It's an authority sorting under the

Swedish Ministry of Finance. And the authority consists of approximately 40 employees and 80 external supervisors. The external supervisors control the lottery draw and spins. Included in some of the external staff is special supervisors controlling the illegal market, the market who hasn't a legal permit. An example of that is illegal slots, illegal poker clubs, and other activities that are not permitted. And if we find any illegal gambling activity, we file a report to the local police and a prosecutor decides if they want to press charges against that person or company.

Sweden's lottery market is regulated and the operators are only permitted to be owned and run by the government, equestrian sports operators, and non-governmental organizations. The business community is, in principle, excluded from the lottery operations and the proceeds from the lotteries are reserved for public purposes and institutions serving the common good.

The Swedish regulated gaming market consists of two major operators that control approximately 86 percent of the regulated market. The first is the state-owned Svenska Spel that offers lotteries, scratch cards, sports betting, and casinos. The other major player is ATG; it's the horseracing and trotting company. And ATG is not owned by the government or the state but controlled by the state since the government appoints six of its 11 board members, including the chairman. The remaining part of the market consists of nongovernmental organization lotteries and small mini-casinos offering Blackjack and roulette. It's a very small scale.

No bank transfer or IP blocking is used in Sweden regarding online gaming. It's not illegal to play on foreign websites, though it's illegal to publish adverts for the foreign sites. Marketing of unlicensed gambling companies is not illegal in Sweden. However, it is forbidden to publish advertisements for unlicensed games in Swedish media or on the Internet or on billboards, thus making it virtually impossible for the unlicensed gambling companies to market themselves.

And briefly, some numbers. Gambling spending per capita over 18 years is €570 per year, and the gambling spending in relation to disposable income is 2.64 percent.

Two major factors have affected Swedish lottery regulations since the 1990s, namely, Sweden's membership of the EU in 1995 and the substantial growth of the Internet during the '90s and beginning of the millennium. Technical developments of the Internet have enabled about 2,000 foreign websites to be accessible for monetary gambling.

This increased the number of Swedes playing on foreign websites, with a consequence that it was not possible to uphold the protective intention of the Swedish lottery regulations. Sweden's accession to the EU entailed EC law becoming applicable in Sweden. Lotteries are not harmonized under EC law but are instead subject to national regulation in all 27 member countries.

In a number of cases, the European Court of Justice has tested issues on conformity between national regulation and EC law. The conformity of the Swedish Lotteries Act with EC law has been questioned by, among others, the European Commission in two ongoing encroachments against Sweden. And the latest case that was legal—it's a Portugal case that said, more or less, it's okay for the state to have their own regulations.

And now to the major—the background on online poker, in February '05, the state-owned company, Svenska Spel, applied to the Swedish government for a license to organize and offer poker over the Internet. The government decided on 24 November 05 to give the company license for the period from December 1 '05 to the 31st of December '07. And Svenska Spel began to offer poker games over the Internet in March '06.

In the first permission, the government decided that an evaluation of Svenska Spel's poker would be done by commission. The evaluation concluded that Svenska Spel had reached the intention of the permission and followed the conditions as well. Some suggestions were given by the commission. All suggestions, except that Svenska Spel, would be allowed to have pool play with

other state-owned poker sites were implemented in the subsequent permit with Svenska Spel.

The permit was extended by the government in November 8, '07, with exactly same conditions until the last of June '08. In December last year the permit was once again extended until last of December this year. Svenska Spel was and still is the only operator that holds a license to offer online poker in Sweden to Swedish inhabitants over the age of 18.

The main reason for allowing online poker in Sweden, even though it is thought to be one of the most hazardous games, was that Swedes already was playing on poker sites with or without licenses issued by other countries outside Sweden. Since all other gaming in Sweden is regulated and controlled through the Gaming Board, this area was uncontrolled. The government realized that online poker was here to stay. And to be able to control and protect the players and to make sure a measurement of responsible gaming was taking place, the government granted the application from Svenska Spel.

The reasons why the government granted a state-owned company were several. The major reason was that the most hazardous types of games need to be strictly controlled and therefore the company received a license. And the legal ground for the poker game is that it's a game of chance, not a game of skill.

In the government permit—they're presented in nonofficial translation in the appendix—the government conditioned the permit with requirement limiting the activity in order to pursue a more responsible gaming. It's also mandated that the Gaming Board to decide about further regulations.

And Svenska Spel took a significant share of the Swedish poker market quickly, as said before. The total number of Swedes, regardless of site, who play online poker appears to have increased steadily until '06 and then leveled off or even decline slightly. The number of Swedes that has played at least once on any poker site between '05 and '07 was estimated to be between 100 and 100,000 persons in the year of '05, approximately 200,000 in '06, and approximately 175,000 in '07. Svenska Spel estimates that it accounts for just

over one-third of the Swedish market, defined as person-based in Sweden playing poker online. In addition, a handful of companies account for approximately 5 to 10 percent each of the Swedish market and the rest is divided among a large number of companies, generally with less than 1 percent market share.

The online poker condition of the Gaming Board are a mix of technical, security, and responsibility to rules. And Svenska Spel's online poker has about 300,000 registered accounts; 25 percent of these play on a regular basis. And the gross turnover and rake for Cashgames, table tournaments, and Sit & Go, in an average in '08 per month was \$239,340,048, and the rake was \$4,495,371. And that's the money that Svenska Spel take; it just takes the rake, nothing else. The rake has declined a little bit until '09 to \$3,469,468.

And some example of governmental conditions:

- It says that the company must allow—not allow—anyone under age of 18 to participate in the poker game over Internet;
- The company shall not allow anyone to participate in poker games if the player hasn't set a limit on how much he or she may lose during a certain period of time;
- The company shall not allow anyone to participate in poker games if the player has not set a limit on how long he or she will play;
- Marketing of online poker is only allowed in newspaper and on Internet, no direct links;
- The company must consider and actively work for the prevention of problems with excessive gambling;
- The company will offer players an instrument that gives the player information about the individual and accumulated losses in Swedish Kronor;
- The company will offer players an instrument that gives the player information about the individual accumulated playing time in minutes;

- When a player first logs onto Svenska Spel's game clients, Svenska Spel must ensure that the player, before he can participate in poker games, receives information about poker's special character—it's a quick game;
- And a maximum bet is two-price amount, approximately \$11,500 U.S. dollar—\$11,500 is the maximum.

And on top of their government's conditions, we have issued condition as well and I will read some of them:

- Those who wish to participate in the lottery must be over 18 years of age and reside in Sweden and be confirmed by a reliable third party; by the same date, confirmation is sent to the participant;
- The license holder shall, on demand, by the Gaming Board leave information about the number of sold tickets—we say *sold* tickets as participants since we have the regulation court through the Lottery Act--number of participants and the age structure, turnover per hour/month and turnover of individual participants;
- Operation and testing divisions shall be separated from each other;
- The verification system shall register the participant's name, address, social security number, or similar, the first time that he participates in the lottery;
- The verification system shall verify that the participant is eligible to participate in the lottery; this includes control of the access codes and the resources available for the game;
- The license holder must have procedures and staff accessible at all times for the handling of complaints and other matters relating to the lottery;
- The license holder must have procedures for detecting fraud, attempted fraud, and authorized collaboration between players;

- The license holder must have procedures for sanctions against players who may be suspected of fraud, attempted fraud, unauthorized collaboration between the players;
- The license holder is not permitted to pay or lend anyone money to participate in the lottery; the license holder ____ that we have issued;
- Another thing is quite important, that the stakes of the game is only against stakes from the players; it's not allowed to have free spins or free wins or anything like that.

SENATOR WRIGHT: Thank you very much. Again, we'll finish this panel and we'll take questions of this panel specifically. I'm going to move—Mr. Söderlund, that was your completed...

MR. SÖDERLUND: Yes. _____.

SENATOR WRIGHT: Okay. And then we have the information about the government decision.

What I'd like to do is move to the next panel. But don't leave because there are a couple of questions that we have, but we'll take all the questions at one time.

So Mr. Stocker, if you would proceed.

MR. ROBERT W. STOCKER, II: Thank you.

SENATOR WRIGHT: Thank you very much.

MR. STOCKER: Mr. Chairman, Committee Members, good morning. Your weather out here is somewhat like Michigan except we have snow.

My name is Robert W. Stocker, II. I'm a member of the law firm of Dickinson Wright PLLC. We have offices in Michigan, Washington, D.C., Toronto, Arizona, and Tennessee, and we also have affiliation relationships recently in Macao. I am a founding member of the International Masters of Gaming Law and just completed a two-year term as its president. And I'm currently the chairman—or chair-elect—for the Gaming Law Committee of the

American Bar Association. I also teach gaming law at the Thomas Cooley Law School in Michigan, as well as several business planning courses.

By way of background, I have quite a bit of experience representing casino developers, casino operators, and casino equipment manufacturers, as well as designing gaming legislation, drafting it, and also drafting gaming regulations, both in the United States and overseas, as well as drafting amendments to constitutions.

That being said, I want to emphasize that I'm not appearing on behalf, before the committee, on behalf of any clients—in fact, my clients don't know I'm here—but rather, I'm here speaking as a professional, a lawyer, who has extensive regulatory experience in the gaming industry and has observed the phenomenal expansion of gaming in the United States and worldwide over the last 15 to 20 years.

Now quite frankly, during the course of today's hearings, you already have heard, and you will continue to hear, and be inundated with statistics, with pro-Internet poker opinions, with anti-Internet poker opinions, problem gaming studies, and other relevant and, frankly, irrelevant anecdotal information regarding gaming in general, as well as Internet gaming in particular. Every position presented to you during this committee hearing will have studies and statistical data used to support that particular speaker's position. I mean, this comes as no surprise.

Frankly, what I am reflecting on, my request to me to come in and talk about what's going on in other jurisdictions, I decided it would be wise to take a slightly different approach as opposed to just, yes, lots of statistics. Now I might add, what's being passed out now is a preliminary draft of what I am working off of. There's actually more to it. My secretary was sick the last couple of days, and so I had to leave Michigan without getting it finished up, and I will be getting a more extensive document to you in email form.

Last spring, I spoke in Washington, D.C., before the North American Gaming Regulators Association. I believe that the California Lottery folks and regulators are members of that organization. And what I said, my theme of

that presentation, is consistent with what I'm going to say today. The reality is that Internet poker gaming train left the station a long time ago and is picking up speed.

While estimates vary widely, it appears that the global Internet poker market is currently around \$15 billion, give or take a few billion dollars. More than half of the approximately 15 million persons who play Internet poker are from the United States—close to 60 percent are from the United States, slightly over 57 percent—and they're playing Internet poker from their homes in the U.S. The remaining poker players, Internet poker players, come primarily, almost exclusively, from Canada and Western Europe. There's very little poker play in Asia at the present time. They play other kinds of games, like pai gow, et cetera.

As I'm speaking to you today, thousands of American citizens, including California residents, are playing Internet poker. That's the reality. They'll continue to play Internet poker today; they'll play it tomorrow; they'll play it next year, next month, next year, notwithstanding the Unlawful Internet Gaming Enforcement Act and notwithstanding periodic anti-Internet gaming pronouncements from the Department of Justice or other actions that the Department of Justice takes.

To me, as I look at what you're looking at and what you're struggling with, in connection with gaming legislation, is the real issue that I think that, the fundamental issue you're facing, is whether or not the state of California, through legislation, decides to harness intrastate Internet poker by licensing and regulating it for the protection of its citizens and, as an offshoot of that, also generating significant, additional revenues for the state. Now regardless of the decision that this committee makes or the California legislature makes, the Internet poker is going to keep on, the train is going to keep on chugging along.

Now what are the primary concerns of the Internet poker player? Because I think that's important when you also think about licensing and regulation. They want honest operators; they want honest games, no collusion; they want easy access to play; they want no bots—that's b-o-t-s—that's robot

play, which is an issue that has to be dealt with, a computer robot play—and they want prompt access to winnings. That's all tied up I one word—integrity, integrity of the game.

Now I've been asked to discuss the international aspects of Internet poker, and I want to lay out kind of a perspective here.

First, it's important to understand, as I said, that Internet poker is primarily a North American and Western European phenomenon.

Second, the European countries, such as Sweden, have been the first to license, regulate, and tax Internet poker. This has been through two separate and distinct processes—state monopolies, such as Sweden, the Sweden approach, and private-sector, licensed competitive sites, such as what is occurring in Italy and France, and I'm going to talk about Italy and France in a couple of minutes.

Now as a result of the European Union's focus—it's kind of complicated in the EU, but the European Union's focus is on cross-border commonality of treatment. And as a result, there has been a great deal of pressure applied by the European Union on state monopolies, to break down the state monopolies, and broaden the access to Internet gaming by cross-border, licensed Internet gaming operators. This is a battle that is going on today. It's going to continue on for the next few years, but it appears that the trend is going against state monopolies and more towards opening up of the licensing online Internet gaming in general.

Jurisdictions, such as Malta, Alderney, Isle of Man, Gibraltar, Antigua, the Kahnawake Tribe in Quebec Province, are the leaders in licensing online Internet gaming in general and online Internet poker.

In my opinion, the licensing regulation and taxing of private-sector Internet poker sites is the wave of the future. It is the clear focus of the European Union in its pronouncements and the European Court of Justice based upon opinions in the taxation area that have been issued by the European Court of Justice. State monopolies are still there, but the force of open environment is gaining momentum significantly in Europe. The

excitement surrounding the opening of the Italian market to competitive Internet gaming sites is an example of what is possible when competition prevails over a monopoly.

Now frankly, I think that makes eminent practical sense. Monopolies create bureaucracies and stifle competition, regardless of whether or not they're a state monopoly or a private monopoly. Competition breeds creative services and marketing which, in turn, generates more business and hence more revenues for the state coffers in the form of regulatory fees and taxes.

Moreover, licensing of private Internet operations places the state in a strong competitive position as additional states open their doors to licensed and regulated Internet poker sites; and, most importantly, as the United States Congress eventually adopts some form of Internet gaming legislation, whether it be something similar to the Barney Frank bill or to the Senator Menendez bill, eventually that will happen. It's not going to happen this year, but eventually it will happen. And I would suggest to you that states that addresses on an intrastate basis first put themselves in the strongest position in terms of addressing the future of Internet gaming, starting with Internet poker and going beyond that as Internet gaming expands in the U.S. A California intrastate Internet poker act that focuses on licensing private Internet poker companies that is up and running when federal legislation is adopted will provide a significant economic advantage to California in the race for Internet poker dollars.

In this regard, as I talk about France and Italy, I want to emphasize that I do not support state monopolies. I support an open, competitive environment. I think that that will generate a great deal more positive impact for California than a state monopoly will.

I want to turn now briefly to Italy which is where a lot of the excitement is occurring right now. The overseer of the licensing and regulatory environment in Italy is AAMS. It's a state regulatory body. I'm not going to try to pronounce the entire name because my Italian is atrocious. But essentially what Italy has done is, it's initially restricted to holders—the Internet poker in

Italy is initially restricted to holders of Italian remote licenses. There are approximately 60 of those companies that have Italian remote licenses, and they can operate Internet poker within Italy. Ultimately, the Italian authorities, AAMS, have indicated that they will expand that licensure beyond the borders of Italy. They charge a license fee. The license is for a specific period of time. Currently the licenses—the currently issued licenses will lapse in June of 2016. There is a dedicated platform that is linked to a centralized system. There was discussion with the last panel about the software programs that are available today to oversee exactly what's going on in the Internet industry. Italy is taking advantage of those programs.

There is a bond requirement backed by substantial bank guarantees required of each licensee. There is a certification that's required by independent auditing firms regarding the existence that require technical infrastructure and management resources. It is open. The Internet poker is open to Italian residents only. That fits in nicely of what you initially start with in California as an intrastate operation. No foreign-based dot.com platforms are allowed. And the software has to be certified. A very, very comprehensive program has been set up by the Italians to deal with Internet poker.

I want to turn to France now briefly. France is also pursuing the same approach. In France, once again, each Internet operator has to be licensed by French authorities. The license is for a specific period of time, five years. There is a heavy emphasis on CSR, Corporate Social Responsibility, focusing on protection against underage gambling, addressing problem gamblers. There is software. The software is in place today and this is being used in, for example, the Atlantic provinces in Canada in connection with slot machines. There is software today that identifies player conduct and enables the overseers, the regulators, to ascertain whether or not compulsive gambling activity is occurring, to ascertain whether or not there is robot play going on, to ascertain whether or not there is collusion amongst players occurring, to ascertain whether or not there is any attempt at money laundering occurring. All of these types of concerns are identifiable with the software that currently

exists. And there's a heavy emphasis, as I said, with Corporate Social Responsibility in the French system.

You also have to maintain a French bank account. That's something I would strongly recommend here in California that, number one, any licensee must have a physical presence in California; its servers must be in California—that makes it intrastate—a bank account must be maintained in California and audit authority of those bank accounts being held by the regulators.

As was indicated earlier in connection with the regulation, a careful vetting of who the owners of the Internet poker site are—a board of directors, officers, and the actual owners—if there are holding companies involved, you go to the holding companies also and then check them out completely and thoroughly. And you already have a structure here in California that is in place that would, in terms of staffing, that would be able to undertake all of that betting. And finally, in France, what they've also done is, they blocked out—they worked hard on blocking out unlicensed iGaming.

At the end of the day, the systems are there and available for you to address the money laundering issues, the chip-dumping, pattern betting, know-your-customer rules, having a state bank account, audit procedures, et cetera, there. The technology is there for the corporate social responsibility issues, including problem gambling and underage gambling. The technology is there to identify robot play, collusion. It is all there and available to you, and it needs to be carefully considered by you and implemented by you in the event that you decide to move forward with the legalization of intrastate Internet poker. And I strongly recommend, if you do proceed with it, that it not be a monopoly system but, rather, that it focus on licensure of a variety—not two or three or four—but a variety of Internet poker sites that come and do business and are based here in California. Thank you.

SENATOR WRIGHT: Mr. Holliday.

MR. SIMON HOLLIDAY: Thank you, Mr. Chairman, advising me to give evidence. I'm Simon Holliday. I'm a director of H2 Gambling Capital which is a UK-based consulting and market intelligence company.

I've only just been called, so I'm just going to provide you with this brief...

SENATOR WRIGHT: Excuse me. Would you come a little closer to the mike? Yeah, that'll help.

MR. HOLLIDAY: Bring it closer.

SENATOR WRIGHT: Thank you.

MR. HOLLIDAY: I've only just been called, so I'm going to just provide you with a brief overview of where we are in terms of the current Internet gaming market and the potential in the future.

A little bit of background about H2, we've been tracking the Internet gaming market since 2003. We are utilized by the vast majority of the listed Internet gaming companies and the vast majority, just about all of the investment banks in London that cover this base. We've provided information to and worked with over 500 clients, our team in the last decade, and we built a speck ?? model which tracks activity on player poker sites across the world, both volume and value, and we're building capabilities into that to look at unique player's play location and that type of thing.

So we look at this market every day. It's what we do, and we've already heard some different numbers; but hopefully I can tie together some of our numbers that are up to date and cover various aspects of the sector.

Two thousand and nine, our view of the global Internet gambling market, prior to companies reporting the actual Q4 ?? results, is that it was worth \$2.6—sorry--\$26.2 billion dollars. That's in terms of gross win, so that's customer stakes, less prizes paid out, but includes bonuses. That includes betting, sports betting, all forms of that. It includes pari-mutuel horserace betting, which is regulated in certain states in the U.S. It's regulated in Japan. It includes commercial sports betting in other jurisdictions. It includes poker, casino, Bingo, lottery games, and state lotteries. In Europe, lots of state lotteries are currently active on the Internet.

Of that, \$4.9 billion was due to Internet poker. That's gross rake, from ring games and from tournaments. It's the fees paid on the buy and the

players, the players, when they pay when they participate. Now of that, we still known that the U.S. is a significant market. It's over \$5 billion of that, of which poker represents about \$1.4 to \$1.5 billion.

The state of California, from the work we've done—and we've had site of activity in California at various times in history. We believe that the market is still worth just over \$300 million, and there's approximately a quarter of a million unique active players participated in 2009. That would mean an average spend, a person, gross ____ before bonuses are taken in consideration, of just over \$1,200, I believe.

So what about our forecast if a market was regulated in California? First of all, I'd say this includes the total potential market in California. We haven't assessed yet the extent to which that offshore activity I just referred to would be repatriated. During early days, we've seen Sweden where we've heard mentioned Deutsche Bank's figures are 40 percent; the regulators' figures are 30 percent of the market being accounted for by Svenska Spel. In Italy, we believe in the current year 2010, once we get ring games, as well as tournaments, provided with many of the offshore operators choosing to have gone within the regulated environment where they had the opportunity to, over 80 percent of that market will be offshore ??.

So until we know exactly what it is involved in terms of the regulation and how it will be policed, we wouldn't want to put a number on that. But what we can say in a commercially regulated market, we would expect in year one that any existing offshore market would double the travel; and by year three, we would expect in California the value of an Internet poker market in total to be \$1.1 billion. This assumes, and based on our constant analysis of poker sites, this would assume round-the-clock average of 17,000 real-money players which, to give you an idea, is about a third of the scale that poker stars ?? currently have. Now it's half of what you see on a poker site because they only cover ring games. But when you include tournaments as well, it's about a third of their liquidity. So I think that, for me, demonstrates the importance, that if you do regulate Internet poker, yes, there should be commercial

competition, but you should be trying to pool activity on one platform to make it as competitive as possible.

Looking at the relationship between numbers of players you have active and number of actual unique players you have, because players tend to have more than one account where they have the opportunity to, we would estimate by year three you would have somewhere between 680,000 and 700,000 adults over 21 playing Internet poker in California. That's about 2.2 percent of the population. Now that sounds slightly low compared to figures we quoted for the UK of 7 to 8 percent, but those figures included for instant gambling so the lottery—it included casino; it included sports betting because everything is available there.

That, I think, includes my overview of the market. I'm happy to take questions or indeed supply written evidence if you feel it necessary.

SENATOR WRIGHT: Okay. We'll take questions from this panel.

Senator Price.

SENATOR PRICE: Thank you again for this panel.

Mr. Söderlund, this is directed toward you. I read somewhere, and the chair made reference to the fact, that when Sweden first enacted its Internet poker law, that you captured about 30 percent of the market. And now I'm told that that there's about an 80 percent capture in the market in Sweden. Can you tell us a little bit about that? What's in the period of that increase and what do you attribute it to?

MR. SÖDERLUND: Svenska Spel has approximately 30 percent of the regulated market or the market, Internet poker market, and the rest is taken by others. So it haven't increased really through the years since our estimation shows...

SENATOR PRICE: You're saying that 30 percent has been pretty constant then? It's not a greater percentage now?

MR. SÖDERLUND: Pretty constant.

SENATOR PRICE: Oh. I misunderstood.

MR. HOLLIDAY: I did refer to an 80 percent but that was at what we estimate Italy this year.

SENATOR PRICE: Okay.

SENATOR WRIGHT: Senator Harman?

SENATOR HARMAN: I had a question for Mr. Stocker.

You talked about the situation in Italy and in France and that they're licensing. What kind of license fees are they charging? Is it a flat-dollar amount or Euro amount. Is it a...

MR. STOCKER: Yes.

SENATOR HARMAN: ...percentage? How is that calculated? And are they not only licensing but are they also taxing?

MR. STOCKER: Yes. They are charging licensing fees. As I recall in Italy, I think it's about €350,000 for the license, if I remember correctly. I've got some notes on it. And in both cases, they are charging a tax. And in France, they've kind of flip-flopped as to what they're charging. But ultimately, at least the most recent pronouncement is, 2 percent of pots as the tax, the state tax.

SENATOR HARMAN: Thank you.

SENATOR WRIGHT: Let me go back. We were discussing a little bit of licensing. Does Italy limit the number of licenses so everyone who gets the license fee can simply get a site in the Italian market?

MR. STOCKER: You still have to—you have to meet the standards—you have to be vetted, an investigation of the proposed licensee is undertaken. And then if the licensee is approved—in other words, they're honest, integrity, they have the right system in place, et cetera—then they pay the license fee and they are allowed to operate the Internet poker site. They only can take in residents of Italy. It's restricted residents.

SENATOR WRIGHT: Different question. I'm sorry. So in Italy, you could conceivably have an unlimited number of sites. So as many people who meet the qualification and paid the fee, they'd have access to opening up a site?

MR. STOCKER: Yes. There is not a limit on the number of sites per se. There are approximately 60 sites now that have licenses from the AAMS. There is the practical reality, that because of the cost of getting the license and the money, investment money, you have to put in to setting up the Internet site, that's going to

have the practical impact of limiting the number, ultimately the number, of licensees that exist because, if you have 10,000 licensees, most of those licensees are not going to have very much business and are not going to survive.

SENATOR WRIGHT: So you would, I'm gathering, you would suggest that you limit the sites by letting the site holders assume that risk rather than the state attempt...

MR. STOCKER: The marketplace.

SENATOR WRIGHT: Okay. Let the marketplace sort it out, yes,

Now I think that that is the most effective way to ascertain. In fact, what is the right number of sites? To just pull out of a hat the number 5, 10, or 15, I think restricts, limits the effectiveness of Internet poker licensing. I think that the marketplace traditionally has proven itself to determine what the stable environment, a proper stable environment, is for Internet poker sites.

SENATOR WRIGHT: So if I'm understanding the risk model that you described, the state takes a licensing fee. I guess that's a like a one time or is that an annualized...

MR. STOCKER: Annualized fee.

SENATOR WRIGHT: So the state takes a licensing fee. So that's—I guess that would be the primary revenue source for the state...

MR. STOCKER: Well, no.

SENATOR WRIGHT: ...and it would—you said it would still get a percentage of each pot.

MR. STOCKER: Let me correct myself, first of all.

SENATOR WRIGHT: Okay.

MR. STOCKER: The license fee in both France and Italy, the license is for a five- or six-year period. So there's a one-time fee for the license. It's not an annual fee but it's a limited time period for the license itself.

SENATOR WRIGHT: Okay.

MR. STOCKER: And then the second thing it has done is, the state does tax each of the sites. In France, originally they were looking at taxing based upon the deposits that were made by each of the players, but they backed off of that because there was strong resistance to it, and their most recent pronouncements are that they

will do a 2 percent tax on the pots as opposed to the money deposited by the players. So there is a tax at the state level as well as a license fee.

SENATOR WRIGHT: Okay. And again, so the state's risk is trying to simply determine how much the value of the enterprise is, say, in France or Italy, so that they take a license fee and they take 2 percent of the pot. They assess that that's their best way to collect revenue for the state?

MR. STOCKER: Yes. Plus, what I would recommend also is, in addition to a license fee, typically what we're seeing nowadays is that any regulatory expense that is incurred, the investigation expense that is incurred, by the state in connection with investigating the licensed applicant, that is charge back to the licensed applicant. That would be a third—that would be a third revenue source but that's just reimbursement of actual expenses.

SENATOR WRIGHT: You mentioned the playing of bots or robots, the concern there being, does the robot play with real money? I mean, because it's a robot, it doesn't have the emotional rigors of playing the game. What would be the concern of having the bot in the game?

MR. STOCKER: Poker is a game of statistics, it's odds. And depending upon the hand that you hold, there are specific odds to—and the number of players and the number of cards left in the deck—there are specific odds as to the likelihood of getting a winning hand. And the really successful poker players are basically statisticians and they play the odds, and those odds can be put into a computer. And robot play is, you're playing against the perfect memory, the perfect odds machine. And the average poker player is not a perfect odds machine. And therefore, it is an unfair advantage. In a robot, you can have a player that's using a robot to make a decision as to a computer, in other words, to make a decision as to how to play the game going forward and tied in with that particular player's play on the Internet site. That has been a problem that was identified a couple of years ago, and there is software now that identifies if robot play is involved and that should be illegal play.

SENATOR WRIGHT: This will sound dumb, and you can tell I don't know how to play poker, but I'm actually in the Alex Padilla School of Poker, and my tuition is going up a little bit. But what would stop someone from having a computer, say, a second computer, while they were playing online poker and do exactly that?

MR. STOCKER: Well, again...

SENATOR WRIGHT: I'm saying, if I'm sitting, playing, I'm in a game and I'm actually playing but I've got a second computer or I've got a co-operating unit in my computer and I'm actually playing—I'm playing just like the robot because I'm using the robot to assist me in my decision. It would obviously be more complicated if I was in a brick-and-mortar facility.

MR. STOCKER: Yes. The answer is that humans are imperfect beings.

SENATOR WRIGHT: Right.

MR. STOCKER: And therefore, that there's imperfect play, and the software programs identify what appears to be perfect play. And that then becomes a warning sign, a signal, that that individual's play needs to be looked at as to whether or not it's fair play or illegal play.

SENATOR WRIGHT: So the...

MR. STOCKER: So it's an identification factor.

SENATOR WRIGHT: So the term of a bot play would also include a live person using a computer assist. That would also be an illegal form of play then?

MR. STOCKER: If the rules and regulations devised by the state say that that is improper, the answer is, yes, it would be illegal.

SENATOR WRIGHT: Okay.

MR. STOCKER: And, for example, in casino play, it's illegal to have, you know, a computer program with you assisting you in connection with playing blackjack, for example. And so it would be a function of the statute and the regulations adopted in connection with the statute in terms of defining what you are allowed to do and what you're not allowed to do.

SENATOR WRIGHT: That's interesting. I mean, I won't dwell on this—it doesn't matter—but how would you, given that no one's in the home and this person is playing, if you said, you played perfectly, how would they determine that you were using the computer? I mean, obviously, if you're in the casino and you had a laptop on the table, then Ray Charles could see that that was cheating. But it would be difficult if I'm in my bedroom and I'm playing and I'm using the—I mean, the only thing might be, if it took me too long to make the play. But the computer could probably make that calculation much faster than I could in my head. So how do you determine that it would be illegal? How do you police that?

MR. STOCKER: Well, if suspicious play is identified, what typically is done is, the play is shut down and the player is shut down until an investigation occurs as to whether or not the player is just a great poker player or whether or not the player is using an illegal means in connection with the, or unapproved means in connection with the, his Internet play, so it's shut down. And that has happened—I will give parallels in the sports betting area. There have been a couple of situations in Europe where there was very suspicious horse betting going on in connection with soccer games, and so the sports bet was shut down. The betting on that particular game was shut down and an investigation occurred. In fact, it was determined that there was illegal play going on, but it was identified by the computer and then was immediately shut down and that's what happens. If suspicious play is ascertained, then it gets shut down.

SENATOR WRIGHT: Now in Sweden, I can market online. If I'm an offshore site, I'm not able to, say, buy an ad on Swedish television or radio or in a commercial newspaper?

MR. SÖDERLUND: That's true in one way. You're not allowed to have, if you own an offshore company, you're not allowed an ad in the television that are sent from Sweden. But in Sweden we have channels from U.K. And since in U.K., they have permission in UK. It's allowed for them to send advertisement in the channel.

But in the newspaper, the newspaper in Sweden, it's not allowed for the papers to publish ads for offshore companies and we try to prosecute them but the prosecutor thinks it's small. The law is not too good. It's illegal to publish adverts for offshore companies, in short, and we try to prosecute them but the prosecutor thinks it's—they have other things to do, they say.

SENATOR WRIGHT: Right. So other than the advertisements that they might do, if I'm, say, the Isle of Man and I'm licensed in Britain, then my play by a Swede would be legal. So if I'm a player in Sweden and I'm playing on the Isle of Man's site, the restriction is the marketing but not the playing itself?

MR. SÖDERLUND: No, it's not illegal for Swedes to play on offshore sites.

SENATOR WRIGHT: Now you mentioned—okay. Well, we may have done that, but the marketing of the online poker is allowed only in newspaper, no direct—what's a direct link? I'm not quite sure I understand that term.

MR. SÖDERLUND: If you click on it, on a link, you end up at, in this case, Swedish Svenska Spel's poker site. That's not allowed. It's like an advertisement who says, don't play on Swedish Svenska Spel.

SENATOR WRIGHT: You'd actually have to search for that site and it goes directly...

MR. SÖDERLUND: Exactly.

SENATOR WRIGHT: ...as opposed to having...

MR. SÖDERLUND: Yeah.

SENATOR WRIGHT: I see. Any other—any questions of this panel?

MR. STOCKER: Could I add one thing?

SENATOR WRIGHT: Yes.

MR. STOCKER: I was asked what the license fee was. I did double check. My recollection was correct. It was €360,000 in Italy, but that is for a license that covers all Internet poker—all Internet gaming—excuse me.

SENATOR HARMAN: Is that the five year or is it €350?

MR. STOCKER: That's the five year. It goes to...

SENATOR HARMAN: So the €350 covers the five years?

MR. STOCKER: Yes, that's right.

SENATOR HARMAN: They don't get a five-year license but pay €350 each year?

MR. STOCKER: No. You don't pay it each year.

SENATOR HARMAN: Okay. Thank you.

MR. STOCKER: It's a one-time fee.

SENATOR WRIGHT: Oh. Senator Padilla.

SENATOR ALEX PADILLA: A couple of quick questions. I have purposely been sort of quiet, a little bit in and out ?? but mainly quiet, because it's an informational hearing, after all, and we're here to learn and to listen. But coming into the hearing, there's a long list of questions. We have the background materials, and the first two that came to mind were, number one, impact on exclusivity clauses in a lot of the gaming compacts. There's been a lot of discussion on that, so I'm not asking you about that right now.

One thing I haven't heard that I did expect to hear thus far—and this is now the conclusion of the second panel—is the jurisdictional question. You know, I chair the

Energy, Utilities and Communications Committee. So when it comes to other things, vis-à-vis the Internet, there's always this question about, well, you can't regulate the Internet. If anybody's got jurisdiction there, it's at the federal level, not the state level. So since this is poker, Internet poker, can you clarify or point to where the state has the jurisdiction to do anything over the Internet and this specifically?

MR. STOCKER: Well, in part, it's a commerce clause issue in terms of intrastate. If the activity is limited to just activity within the state, the commerce clause does not come into play. An interstate, when you have interstate commerce, then the federal government steps in. But if it's all intrastate, then the state has the right to regulate that. There is within UIGEA, there is some language about intrastate gaming activity and which seems to point to the concept or the idea that, yes, you can have intrastate Internet gaming.

Now the feds, the Justice Department, has made a couple of pronouncements saying they don't agree with that, with that concept, but there has been no litigation which has specifically resolved it in any federal court saying that intrastate Internet gaming is illegal or cannot be done.

SENATOR PADILLA: Okay. Just to highlight that question, the other question right now kind of prompted by the chairman's description of a player sitting at home and using a computer and, you know, poker's just a different kind of game. Why are we not having an intrastate Internet Blackjack conversation?

MR. STOCKER: It's a good question actually. The main reason is because, what's happened over the last four or five years is there's been an explosion of interest in poker that frankly commenced with these poker tournaments that were being run in Las Vegas that were being televised. And that has, the interest in Blackjack has gone down and interest in poker has gone up. It also—and I agree with some of the panelists of the first session—that it is more of a young man's game—it's about 75 percent men, 25 percent women—and it's very much statistical, and it is a game that we all play. I mean, as a kid growing up, I didn't play Blackjack because you're playing against the house. I played poker because I was playing against my three or four friends. So it is a fundamentally different game than blackjack where you're playing against the house. Instead, you're playing against your friends or, in this case, in the Internet you're playing against

either, you know, a random computer or else you're doing, you're playing a game that is a, that's a tournament where a whole bunch of people are involved in it.

SENATOR PRICE: That's just my roundabout way to shine a light on the question of robot play being unique, given the nature of poker itself—that's, most players will say...

MR. STOCKER: Yes.

SENATOR PRICE: ...it's not just, you know, what the best odds are in this hand. There's an art to it.

MR. STOCKER: You know, and something else I would add in here, when people were talking about projecting on how many people are going to be playing, a comment was made by one of the persons in the first group in terms of Internet, why, you know, international sites and, well, still the focus being the international sites rather than intrastate. Well, I tend to disagree with the idea that the Internet, international Internet sites, will continue to be the dominant player. I think that once the intrastate Internet poker is legalized, what is going to happen is, is that major casino operators, who have already looked at Internet gaming but are not doing it in the United States because it's still in a grey area, is that what they will do is, they will start sponsoring poker tournaments, intrastate poker tournaments, run an intrastate site with, you know, a server based in this state where they're licensed.

And as part of their marketing, it will mean not only win a pot but also, you know, win the game but also win the right to come to a tournament in Las Vegas, comps in Las Vegas or wherever, or, you know, the tribal casinos here doing comps in the tribal casinos. You'll have all those kinds of marketing events which the international Internet operators cannot, you know, provide. And as a result, the combination of those marketing tools, plus honesty, integrity not worrying that some Russian is running off with the money, will cause the majority, the substantial majority, of the players to gravitate to these licensed, legal sites, in my opinion. It's part of education—it's an education element—but that is what will happen if you proceed forward with intrastate Internet poker, in my opinion.

SENATOR PRICE: Thank you.

SENATOR WRIGHT: Any further questions of this panel?

Gentlemen, thank you so much. It provided a lot. Mr. Simon ??, we'll probably, if you could summarize, we'll make some of the folks who brought you will highlight a little bit of what you've said. We've got it in a video form, but we might want to compile some of that for a period later on. Thank you all so much.

MR. STOCKER: Thank you.

SENATOR WRIGHT: We're going to go to Mr. Appelsmith from our Bureau of Gambling Control, and then we're going to take a short break after Mr. Appelsmith, and then we'll try to resume literally in about 30 minutes and come back and finish the panel. I appreciate the attention and the patience that everyone's had, and I know there's been a whole lot of conversation, but I hope that the information is useful to everyone who's here. Thank you.

Mr. Appelsmith.

MR. JACOB A. APPELSMITH: You're welcome. I'm Jacob Appelsmith. I'm the chief of the California Bureau of Gambling Control and a special assistant to Attorney General Jerry Brown.

I want to talk briefly about the concerns from the standpoint of state regulators. This is a very complex question obviously from the people of state of California, for tribal governments, for card room operators. There are really three ways of looking at this.

One is the status quo, which is that we have a billion-dollar industry as to which we're doing absolutely nothing. There's no policy; there are no specific laws; there's no regulation in this state. There's no revenue for California businesses; there's no jobs for Californians; and there is no revenue for the government.

A second way we can look at this, whether we're going to legalize something or not, is from a compliance enforcement standpoint, which is to adopt specific laws and address Internet gambling and to put enforcement measures in place to try to support those laws.

The third measure, of course, is what this committee is primarily looking at today, which are possible models for legalized Internet gambling. There's open licensing to California and foreign corporations; there is models that say it should be limited to the current licensees and others operated to actually authorize, offer Internet poker, and that would be California tribes and card rooms. There's

models that say we should have a state-sponsored program, and then there's combinations of the above.

The attorney general does not advocate any particular position on this, other than to say that we believe that the status quo is not acceptable, that something has to be done, whether it's purely enforcement or whether it's some form of legalization. And here's some facts on which I based that. Californians are wagering hundreds of millions of dollars a year as a black market and as a growing market. No one in California is making any money off of this—not those that we've given licenses to, not those we've entered into compacts with. It's just money that's being sucked overseas and is leaving our economy every day, and this is one area where we ought to be able to control that in some measure or another.

The public is not protected. There are documented histories of cheating scandals that are either operated by the sites themselves, that are operated by people who are able to infiltrate them because they have weak security; there are companies that seize player pools and disappear; and then there are players who plain just cheat online, and California has no way to detect whether any of that is occurring because we don't regulate or monitor it at all. So I thank this committee more than anything for trying to get out in front of this issue.

Let me talk about it briefly from one of the two perspectives that involve us, which is compliance and enforcement.

One thing we can do is public awareness and prevention. Right now, there's not a lot of knowledge in the public at large as to the fact that this is illegal and the fact that it creates addiction problems, that there's services for those people, and that they can get ripped off and how exactly they can get ripped off.

The second thing we can do is straight-up criminal enforcement. We can make this specifically illegal under California law, and we can go out and arrest people. It's probably not a very good tool, given that the people who are really profiting, that we want to target the most, are all offshore and we would not think that it's an effective model to search people out in their homes and arrest them for playing Internet poker. We can try to tax them; we can try to collect tax. That may have some effectiveness; although again, it's going to be difficult to detect,

costly to do so. There probably is some deterrent factor if we are able to target particularly egregious individuals.

The most effective way to deter illegal Internet gambling from a law enforcement perspective is asset forfeiture and seizures. When you gamble online, the predominant way that people do it is through accounts set up in U.S. financial institutions. So think of those accounts as a cage. You go up; you buy your chips; your money sits in that cage and you get chips; you get out and play; and then when you're done playing, you go out and cash them in. Those cages, those virtual cages, are actually predominantly in U.S. financial institutions. There's other models. There's still some credit card play, although that's more difficult. There are still local operatives who will cash you in and out by hand, although that's less common. But most of the money, as far as we can tell, is sitting in U.S. financial institutions. Our agents can track where that money goes. And in cooperation with the Federal Bureau of Investigation and the Internal Revenue Service, we can go after that money and seize it.

That has proven to be effective by the state of Washington. It's the pioneer in this area. It's the only state that has a full-time dedicated staff to doing this and that has a consistent mission to systematically go after Internet gambling company accounts in the United States. In the last five years, they've seized \$256 million from those accounts, and that money has gone to the state of Washington for prevention and enforcement programs. It's also been shared with the federal government pursuant to asset forfeiture laws under federal schemes.

The state of Washington has been so successful, that many sites now state that they are not open to Washington residents. Now that's not something they actually enforce, but they're concerned enough about the state of Washington that they don't want people playing on their sites. I am confident that we can set up that type of an enforcement mechanism here and make a significant dent in the attractiveness of California as an Internet gaming destination for criminals.

From a regulatory standpoint—let me say one more thing. There's been some discussion of whether we can have virtual borders around California. Are there ways to block sites? An easy example is, California Department of Justice, if I go on a site to look for something that's banned to me, such as pornography, it

blocks me. There are ways to do that within jurisdictional borders of states. There's a lot of skepticism as to whether they can really be effective. There's nowhere in the United States where that's actually been tried successfully. There are providers that say they can overcome the technical and the legal obstacles to doing that. We have done some review of them. We think it is worth exploring. We are somewhat skeptical, but we think that it is something that is worth at least pursuing to see if we can make a material difference in the amount of or the ease of access of California to illegal gambling sites, either under a model of prohibiting it altogether in the state of California or some legalized system that we would want to protect through deterring illegal options.

From a regulatory standpoint, the Bureau of Gambling Control already has a very sophisticated and extensive licensing process that we go through for owners of card rooms, for vendors, to card rooms, and to tribal casinos, to key employees of gambling establishments, and do criminal background checks. We are always interested in whether there has been illegal gambling or gambling cheating in those profiles of individuals that we're seeking to find suitable to do business in California. That would be an issue for any lawful system here as to whether you're going to let in outside providers who've already been engaging in essentially what is criminal commerce for the state of California.

We would need in any regulatory scheme to set up security measures, in terms of software, underage gambling. We have existing systems that allow people to exclude themselves and that give us the ability to exclude them involuntarily from gambling. We would want to tie into those systems and work with the Drug and Alcohol Prevention programs to do that. We would look to see ways we would be able to avoid money laundering and other criminal activities that are commonly associated with gambling and that have made gambling one of the most closely regulated industries in the state of California.

So those are my comments. I'm happy to answer any questions for you.

SENATOR WRIGHT: Senator Harman?

SENATOR HARMAN: I wanted to ask a question about the asset forfeiture and seizure. You said that that would probably be the most effective way to

enforce, but I also thought I heard you say most of the players put their deposit into a virtual cage that's in a European bank.

MR. APPELSMITH: U.S. bank.

SENATOR HARMAN: What bank?

MR. APPELSMITH: U.S. bank.

SENATOR HARMAN: Oh, I thought you said European bank.

MR. APPELSMITH: I'm sorry.

SENATOR HARMAN: So the regulators in Washington, for instance, are able to somehow go after that bank and seize the money on deposit in that U.S. bank?

MR. APPELSMITH: Correct. And the reason that you need the FBI and the IRS is that those banks are rarely in the state where the illegal activity is occurring. There's a rare exception where Washington actually had Washington banks and it was able to do the entire thing without federal cooperation.

SENATOR HARMAN: Okay. Thank you very much.

SENATOR WRIGHT: In California, what specifically is illegal? Is it illegal to do the financial transaction, or is it the play itself that's illegal?

MR. APPELSMITH: There's some debate about whether it's currently illegal to sit down at your computer and play poker under state law. We take the view that it is illegal to do so, just like it would be to play an illegally operated poker game. So essentially there's only three ways to play poker or four ways to play poker legally in California. You can go to a travel casino; you can go to a card room; you can go to an authorized charity event; or you can play in the privacy of your own home, as long as it's not an operation essentially for profit. But there are illegal card games that are run out of bars, that are run on circuits. And we view everybody participating in those games as committing a crime under California law. And we do arrest the players as well as the providers of the games. So they are now playing poker; they're just not playing an illegal game where the person making a profit out of it is also sitting in the state with them.

SENATOR WRIGHT: So if I were online playing poker in a training site that did not involve real money, that would still be illegal?

MR. APPELSMITH: If it doesn't involve real money, it would not be illegal because you're not playing for consideration.

SENATOR WRIGHT: Okay. So the consideration is what makes it illegal?

MR. APPELSMITH: Yes.

SENATOR WRIGHT: Okay.

MR. APPELSMITH: Well, the consideration and the fact that people are playing designed for someone to be making a profit by running the game. So if you and your friends just want to get together and play a friendly poker game in your living room, as long as someone is not running the game to make a profit, it can be lawful.

Now what I said earlier, that if we're going to really regulate this and enforce it, we need to be able to have laws that specifically outline Internet poker because there are some debates about the law enforcement view that I just took. It's not as clear of a statutory scheme as it should be if we're actually going to meaningfully enforce prohibitions against it.

SENATOR WRIGHT: This is almost rhetorical. If six guys get together on Friday and they each bring \$100 and everybody shares the beer and the pizza, whatever it is you bring, and you rotate this game among different guys' houses and chances are, I think, in that exchange, usually the women win but that's another discussion. (Laughter) But that would not be illegal because there was no profit being made by anyone and they were mutually agreeing to play?

MR. APPELSMITH: That's correct.

SENATOR WRIGHT: Okay. Any other questions of this witness?

Okay. We're going to resume at 1 o'clock. We'll be back here at 1 o'clock sharp and we'll start again.

*** Break ***

SENATOR WRIGHT: We're going to get going probably in the next couple of minutes. I just wanted to get a couple of folks in and we'll get right up. Welcome aboard, everybody.

The second part now—it is now 1:07 or 1:0-something, depending on what kind of watch you have, but we want to resume as quickly as we can. We've got the next panel in place and we're ready to go. We need at least a couple of members to get us going.

***** Pause *****

SENATOR WRIGHT: ...I mean, because I know somebody bet on that 4 o'clock time, so I don't want to, I don't want to skew the time. But, again, we're still recording. So if the members are looking on television or in your offices, we will start at 1:20, come hell or high water, or I hope neither of them occurs. So you'll take the water? Okay.

UNIDENTIFIED SPEAKER: _____.

***** Pause *****

SENATOR WRIGHT: We don't need a quorum and we'll take people as they're going. I may have members watching on television. So let me remind the people on the panel, that while there may only be a couple of us on this side, there are a number of people who are watching, and we may even get to sell this because somebody may say something that's like so entertaining that people want to buy it and the state can actually make revenue from selling the DVD. So we're looking for that entertaining clip that we're able to put forward.

But let me welcome all of the tribal leaders that are here.

And Ms. Oropeza who just came in, right there on cue, Senator, welcome aboard.

We spent the morning discussing Part A. This is a panel of tribal leaders, in addition to George Foreman—and we did comment earlier that I've

met George Foreman. In spite of what you said, you're no George (laughter)—but let me welcome Chairman Martin of the Morongo Band of Mission Indians. And it's at 1:20. Sir, that time having arrived 20 minutes later than we said. We're going to get going. Thank you very much for being here today.

MR. ROBERT MARTIN: Thank you, Chairman Wright.

SENATOR WRIGHT: Hit your mike, sir. There you go. Oh, you just turned it off.

MR. MARTIN: I turned it off? Is that better?

SENATOR WRIGHT: Yep.

MR. MARTIN: Okay. Thank you, Chairman Wright and Committee Members, for your time. I know how valuable your time is to you and we appreciate this informational hearing that you've put on.

For the last year, Morongo's taken a lot of time to understand this, as I know you have as well. I understand that you weren't a poker player; you didn't know much about poker; and you've taken a lot of time to understand it over this last year and I appreciate that.

Poker is a game that's authorized by the state and is played through 80, 90 jurisdictions in the state, all across the state, and today I want to talk about—I want to make three points—Internet poker and I want to talk about consumer protection and regulation. Right now, as it stands, there is no regulation for Internet poker.

I've talked to many gamers that come to our casino and some of their biggest concerns are, if they get in the game and they play and they win a pot, they're not guaranteed that they're going to get their money if they win. That's a big concern of theirs and yet they still play, so there needs to be protection for unscrupulous operators to protect the consumer. We understand that Visa and MasterCard [sic] is starting to not allow these transactions to take place.

The third thing that I wanted to talk about is the income stream. There's billions of dollars that are being wagered in California alone. Each week, there's a million Californians playing this game, Internet poker, and we understand through the innovation study, \$13 billion a year is being wagered.

All that money goes offshore to the Isle of Man, to Gibraltar, and other sites. Not one dime stays here with the state of California. There's no taxes being paid to the state. Every penny goes offshore, and we feel that it should be taxed. It should be regulated and it should be taxed.

Then I want to talk about expertise. The tribes have been in gaming for the last 25 years. We started with a bingo hall, built that business from a very small bingo hall to one of the largest and most successful casinos in California, and we wouldn't have built that casino without having the player protections in place. And it's important to understand that, without that, I think that's integral in the game, the player protection, and we should, we feel, that the games should be controlled by the tribes and—by the state and—taxed and it should be operated by Californians and the income streams kept here in California and not gone offshore.

Another thing that we need to talk about is the exclusivity. We hear there's a lot of talk about that. I've brought with me here today George Foreman. He was with us 25 years ago when I was chairman then, and our case went to the United States Supreme Court that started this with high-stakes Bingo. He's here today to ask, to answer any questions on constitutional questions that you may have.

George?

MR. GEORGE FOREMAN: Thank you, Chairman Martin, Mr. Chairman, Members of the Committee, I will be brief.

We have heard, as chairman Martin indicated, people make reference to threats to tribal exclusivity from online poker. The committee, I think, has received a couple of letters—one from Mr. Genest, another from, jointly the CTBA and Pechanga—suggesting that this would somehow breach tribal exclusivity, but we've not heard any substantiation for that claim other than the statement of the claim. And the answer to the claim is really quite simple and straightforward.

First, tribes have no exclusivity with respect to poker. Poker is a game that is lawful in California, for Californians, and the legislature is fully capable

of prescribing how that game may and not be played, including online. In April of 2008, the Legislative Counsel issued an opinion to that effect and I agree with that opinion.

Second, the Constitution allows slot machines and banked or percentage card games only on Indian lands and then only pursuant to tribal-state compacts that are in effect. Poker is not a banked game. It is not a percentage game. It is a round game; and, therefore, is not subject to compact.

Third, the compact defines a gaming device, a little bit different than the Penal Code defines a slot machine, but the definition is a slot machine in various iterations. But a slot machine, in whatever form, is a bank game, a house bank game, or, at very least, a device that determines game outcome and enables either the player to win a prize or the house to keep the player's money. In online poker, there is no gaming device. I have my gaming device in my briefcase. It's called a laptop. You all have gaming devices. They're not gaming devices, is my point. The only thing that the website's computer or server does is shuffle the cards and deal the cards. The players play against each other. They don't play against the machine. They don't play against the house. The players' computers don't apply an element of chance or determine game outcome or award a prize or take money from the player as the result of the outcome of the game, and this too is consistent with the opinion that the Legislative Counsel issued in April of 2008.

So in short, I don't think there is an intellectually defensible, legally supportable argument that online poker, as poker is played under California law, not with a rake of the pot, because that's a percentage game, but charging in the same way that card clubs charge their players to participate in poker games under California law could constitute a breach of the so-called exclusivity provisions that we've heard about thus far. Thank you.

Mr. Chairman?

SENATOR WRIGHT: Thank you, George.

MR. MARTIN: Thank you, George.

So in closing, we would urge that you regulate interstate ?? poker—Internet poker—and that you tax it as well and keep that income stream here in California, don't let it go offshore, get California its fair share of the income, and keep it here in California.

In closing, I want to tell you a story about consumer protection, just to drive that home. A couple of years ago, Morongo had a game that we were playing. It was a promotion that we did, a million-dollar game, and you had to reach a level to get to this game; then you got one pole on the slot machine, and sevens had to come up to win. And one evening, a gentleman from LA came up. He pulled the slot machine. The first tumbler came in, locked in on the 7. The second tumbler came around and locked in on the seven. A third tumbler came around—hit, dropped back, and then came down on the seven. The whole floor erupted, even our staff. They thought it was a win, but it didn't lock in place. It kind of tumbled, but it appeared to be a win. The decision to pay came all the way to the tribal council. We didn't want it to appear to be a bad game at all. It was a malfunction of the machine but we paid that. That's the kind of game that you get at Morongo. That's the honesty and the integrity that you get when you contract with Morongo, and that's what you would get if you contract with Morongo in Internet poker. Thank you.

SENATOR WRIGHT: Thank you, Mr. Martin.

Again, with this panel, as with the others, we'll hold all the questions until the end. So if you stay with us, I'm going to ask Mr. Tucker...

MR. DANIEL J. TUCKER: Right.

SENATOR WRIGHT: ...if he would take up where Mr. Martin left off.

MR. TUCKER: Well, good afternoon, Mr. Chairman and Members, and distinguished guests.

I'm Daniel J. Tucker, chairman of the Sycuan Band of the Kumeyaay Nation, and also I am the just reelected California Nations Indian Gaming Association's chairman.

Internet poker is one of the biggest issues facing tribal governments this year. This is a complex topic with many difficult policies and fiscal questions

that remain unanswered. Even though we're getting a lot of answers today, it's been very, very enlightening to me.

CNIGA has been reviewing this issue since June of 2009. CNIGA opposes the full-blown expansion of casino gambling online as proposed by Republican [sic] Frank and Senator Menendez. CNIGA has reviewed and discussed various proposals relating to limited intrastate Internet poker. The association has not taken a position on any of these proposals as of now. CNIGA is committed to careful examination of all the issues and will continue to discuss the issues with our membership until a consensus can be reached on the best way to move forward for both our tribal governments and the state of California. CNIGA has long opposed any expansion of gaming outside of the promises made by Propositions 5 and 1A.

At a minimum, our association knows this: Any proposal that is brought to the legislature must contain strong player protection, an enforceable regulatory system, a way to ensure minors are not permitted to wager, as well as the protection of our tribal state gaming compacts. Any proposal that is brought to the legislature must recognize the exclusivity that tribal governments negotiated with the state in the tribal-state gaming compact negotiation process.

CNIGA's views on this issue of Internet gaming as complicated—excuse me. CNIGA views the issues of Internet gaming as complicated and challenging. At a minimum, protection of gaming public in California, protection of existing gaming compacts between sovereign tribes and the state is of utmost importance.

CNIGA will go back, Mr. Chairman, and really take a look at what we heard today in this hearing and go back to our organization this next week or so and really discuss what the position is going to be that Cal-NIGA will take. We're very interested in what happens today. And if you have any other questions for me, I will be here to answer them. Thank you so much.

SENATOR WRIGHT: Okay. Thank you.

Again, we're going to hold all the questions. I'm going to move to Mr. Clarke. See, I did that. See, you weren't paying attention. See, I was trying to...

Okay. Mr. Clarke, welcome aboard.

MR. GERALD CLARKE, JR.: Good afternoon. My name is Gerald...

SENATOR WRIGHT: But you've got to turn your—there you go; there you go. It's all right now.

MR. CLARKE: My name is Gerald Clarke, Jr., and I am an elected councilman for the Cahuilla Band of Indians located in Southern Riverside County. I also serve on the board of directors for the California Association of Tribal Government.

I want to thank Chairman Wright, Vice-Chairman Harman, and this committee for the opportunity to testify on behalf of the member tribes of CATG about the public policy and fiscal implications that the authorization of intrastate Internet poker in California, referred to as iPoker, may have on CATG member tribes.

CATG's mission is to promote the understanding of tribal sovereignty, self-determination, and economic means of tribal governments, and to amplify California tribal government voices so we can be heard by federal, state, and local governments. Established in 2008, CATG is *the* largest intertribal association in the state. CATG services are offered to all tribes in the state. A list of CATG member tribes is attached to the testimony submitted previously. CATG's member tribes are diverse. While a minority of gaming tribes are members of CATG, the majority of our members consist of the tribes whose primary source of revenue is the revenue-sharing trust fund of the 108 federally recognized tribes in the state; 71 tribes receive RSTF payments. Of the 71 tribes, only seven tribes operate small casinos with less than 350 gaming devices, and 64 tribes in California offer no gaming at all.

Despite these facts, many continue to view all California tribes narrowly as gaming interests rather than as tribal governments with broad responsibilities, as government's tribes have to address issues similar to those

this legislature faces on a daily basis—water, roads, public safety, land use, communications, social services, healthcare, environment, revenue, and taxation—are all issues we deal with. In addition, tribal governments have interests that are unique, such as preserving and protecting our tribal sovereignty, cultural resources, sacred sites, gathering, hunting, and fishing rights. Tribal government gaming has provided tribes with a much-needed revenue stream to fund their government programs and begin non-gaming economic development.

In addition, tribes in remote locations who operate small casinos have been able to create jobs for their tribal members and their local communities. Non-gaming tribes have strengthened their tribal governments through the revenue-sharing provisions of the California compacts. California tribes were the first in the nation to share gaming revenues with non-gaming tribes. The great majority of the tribes in California are unable to establish a gaming enterprise because of their remote location or lack of a land base. These revenue-sharing funds represent an important means to strengthen tribal governments. As such, all California tribes have an interest in preserving and protecting government gaming.

The purpose of today's informational hearing is to examine the public policy and fiscal implications that the authorization of iPoker in California may have on its citizenry and its economy. CATG has not taken a position with respect to iPoker or the proposal championed by CATG member tribe, the Morongo Band of Mission Indians. CATG has provided relevant information to its member tribes and forums where they can discuss these and other proposals. CATG believes any form of iPoker should serve the public policy established when the people of California gave tribal governments the exclusive right to offer casino-style gaming through their overwhelming approval of Proposition 1A. Should iPoker become a reality, we believe it must be offered in a way that protects the public policy mandate to benefit all California tribes, not only gaming tribes but also non-gaming tribes, who are reliant upon payments from the revenue-sharing trust fund. In the past, decisions have

been made which have had impacts on the interests of all tribes, even though not all tribes were involved in the decision making. This is why CATG must have a seat at the table when the question of iPoker is being discussed and decided.

CATG is mindful, that as these iPoker discussions proceed, our interests may be impacted in ways that may not be apparent today. Therefore, CATG will continue to remain at the table to actively participate in the dialog and decision-making process.

In conclusion, the California Association of Tribal Governments will continue to engage with all tribes in California, the legislature, and the governor in this issue which is of great importance.

I thank Chairman Wright, Vice-Chairman Harman, and members of this committee for the opportunity to speak on behalf of the California Association of Tribal Governments. We stand ready to work cooperatively with this committee on such an important issue. Thank you.

SENATOR WRIGHT: Thank you very much. I'm going to keep moving because there will be some questions for this panel.

And I want to move now to Leslie—I don't want to mispronounce—I hate doing this.

MS. LESLIE LOHSE: Lohse.

SENATOR WRIGHT: Lohse. Okay.

MS. LOHSE: Thank you very much, Mr. Chairman, and good afternoon, Mr. Chairman and Members. I am Leslie Lohse. I'm the chairwoman of the board of directors for the California Tribal Business Alliance, and I'm here today to speak on their behalf.

Our concern is about making agreements and honoring commitments. This state, this governor, and this legislature has entered into tribal gaming compacts with 66 California tribal governments. Each and every one of those compacts in which the state agreed only federally recognized Indian tribes can offer what's called gaming devices to the public. This is consistent with the direction given in an overwhelming vote by the California voters in 2000. And

yet, we're here today to consider the authorization of the play of poker on Internet-connected devices in direct violation of those agreements with the tribes.

Since 2004, tribal gaming compacts have required tribes to make hefty payments to the state's General Fund. Those compacts would not have been approved by the federal government if the tribes' ability to earn enough money to make those payments was not protected in the agreements. As a result, even in a down economy, California tribes are paying to the state \$1 million a day to the state's General Fund. That's \$365 million last year, at least \$365 million next year. That means billions of dollars between now and when the compacts expire in 2030, and that doesn't even count the millions of dollars that the individual tribes pay to the local governments.

If the state were to allow a non-Indian business to offer gaming devices, the compacts provide that the tribes will stop making those payments to the General Fund. I'm glad Mr. Clarke mentioned the revenue-sharing trust fund because much of the money used to make revenue-sharing payments to the tribes that do not operate casinos would also stop if the state were to authorize Internet poker. Internet poker can be played by one person at home, or it can be played on banks of Internet-connected devices lined up at a downtown card club.

Proponents of the Internet poker can argue that the Internet-connected devices aren't illegal slot machines under the Penal Code, or they can include a Penal exemption for the devices just to make sure. They might also argue that such an operation wouldn't violate the state constitution. But what they can't change are the terms of the compacts, which very clearly define a gaming device, and that definition very clearly includes the play of poker on an Internet-connected electronic device.

I'm glad Mr. Foreman doesn't think Internet poker as proposed is a breach. But since we're not paying for that opinion, we believe that a gaming device includes an electronic device that allows an individual to place a bet, play of a game of chance or skill, and view notification of any winnings. It

doesn't matter if the game is house banked or whether the winnings come from the bets made by the players, as in poker. It doesn't matter if it's Class II or Class III. Those definitions do not apply. What matters when we talk about breaching the tribes' exclusive rights to offer gaming devices is that the electronic device allows a player to connect to a system, make a bet, play the game, and view his entitlement to any winnings.

That includes a personal computer in a private home. It includes a bank of Internet-connected computers in a card club which is exactly why card clubs are behind that legislation that was proposed last summer and appears to be resurfacing again this time.

The card clubs, as you recall, back in 2004 tried to get the voters to authorize 30,000 slot machines in urban casinos. The four card clubs behind the Internet poker bill last summer collectively spent \$12 million on the 2004 slot machine initiative. It failed when nearly 84 percent of the California voters voted it down and rejected the idea. So now the card club rooms are trying to come in by way of the back door what they couldn't get in the front door five years ago.

Card clubs, I should note, do not contribute anything to the state's General Fund. Their payments to the state only cover the cost of state regulation. If they were here today saying that they are willing to pay 10 percent tax on future Internet poker winnings, how about applying that same tax on the current earnings right now? Last year, they grossed \$889 million. At whatever rate you might want to propose if you're looking for a deal, there's a sizeable revenue there for the state.

You've heard several estimates about how much revenue the state might expect from legalizing Internet poker. At CTBA, we did look at it. And as Mr. Foreman stated, we had a study done. And based on data specific to California online poker players that we applied to existing models in Europe, \$15 (million) to \$20 million initially is a reasonable estimate, in our view. But whatever estimate you want to consider to be reasonable, you can be assured of the loss

of \$365 million because there is no doubt that state authorization of interstate [sic] Internet poker violates the state's agreements with the tribes.

We're all aware of the federal legislation to legalize and regulate Internet gambling. Those bills—they won't go through this year in Congress, but we all know that they'll be back after the November elections. How the state and the tribes deal with federal authorization for Internet gambling is an issue separate and apart from what we're here today discussing, which is state authorization of intrastate Internet poker. And that gets me back to what I started talking about, is making agreements and honoring commitments.

The ink is not even dry on the last two compacts that were signed, and every member here was supportive of that in December and January. Both of those compacts did have exclusivity clauses. Many of you voted for the 2004 and 2006 compact amendments. Those compacts have exclusivity provisions. In December, the Ninth Circuit Court of appeal upheld the tribal exclusivity provision and dismissed a lawsuit brought by a card club challenging the 2004 tribal compacts. It's amazing to us how quickly agreements and honoring commitments go by the wayside when tribes seemingly have the better end of the stick.

When the 1999 compacts were ratified, the agreement stated, and I quote: "The state enters into this compact out of respect for the sovereignty of the tribes, in recognition of the historical fact that Indian gaming has become the single largest revenue-producing activity for Indian tribes in the United States; out of a desire to terminate pending 'bad-faith' litigation between tribes and the state; to initiate a new era of tribal-state cooperation in areas of mutual concern; out of respect for the sentiment of the voters of California who, in approving Proposition 5, expressed the belief that the forms of gaming authorized herein should be allowed...."

It goes on further to state: "The parties are mindful that this unique environment is of great economic value to the tribe and the fact that the income from gaming devices represents a substantial portion of the tribes' gaming revenues. In consideration for the exclusive rights enjoyed by the

tribes, and in further consideration for the state's willingness to enter into this compact, the tribes have agreed to provide to the state, on a sovereign-to-sovereign basis, a portion of its revenue from gaming devices.”

So there it is. Barely ten years ago, we negotiated and believed together that our agreements would be honored. But here we are today, discussing your consideration of authorizing play of poker on Internet-connected devices in direct violation of those agreements with our tribes.

Speaking on behalf of the member tribes of the California Tribal Business Alliance, we say, your time is better spent looking for other ways to address the budgetary challenges of California. This avenue is one that is filled with too many issues and looks to cost California millions of dollars each year ending in billions by 2030. Thank you.

SENATOR WRIGHT: Thank you.

And we will move to Chairman Macarro.

MR. MARK MACARRO: (Untranslated Comments.)

Good afternoon. My name is Marc Macarro. I'm the tribal chairman for the Pechanga Band of Luiseño Indians.

SENATOR WRIGHT: I was worried for a minute. I thought my drugs were kicking in. (Laughter)

MR. MACARRO: They are. And with all due respect, Mr. Chair, what are you referring to? (Laughter)

Okay. Chairman Wright and Members of the Committee, first, on behalf of the Pechanga Tribe and the nearly 4,000 employees of the Pechanga Resort & Casino, I want to thank you for the opportunity to address the committee on this important subject.

Although Pechanga appreciates this hearing, I must say that we do regret having to speak against this proposal which is largely backed by our friends at Morongo. Despite our historic alliance, this is one of those rare instances in which we simply do not agree with the consequences of authorizing intrastate Internet poker. Morongo and Pechanga—we've been through many battles

together and we agree probably on 95 percent or more of policy issues. But on this one, we don't.

Mr. Chairman and Members, March 7th, this year of March 7th, will mark ten years since the voters of California historically and overwhelmingly approved a constitutional amendment to permit Class III gaming on tribal lands. I trust that every member of this committee is aware of the considerable progress voter approval of Indian gaming has brought to virtually every single tribal community in this state, including non-gaming tribes. We are very proud of the fact that, through the end of 2009, non-gaming tribes received more than \$641 million through the Revenue Sharing Trust Fund. No other state in the union has such a far-reaching and innovative revenue-sharing provision.

Pechanga first began our gaming operations in 1995 with the opening of the Pechanga Entertainment Center. We opened in temporary facilities with only 135 employees. Today the Pechanga Resort & Casino employs close to 4,000 people. If you had visited our reservation in 1995, you would have seen families living without plumbing, families in homes with plastic in place of glass windows; half of our tribal members were living in poverty, and that was then. Today, because of tribal gaming, we fund important governmental services and programs. We provide essential services to our citizens, including our Pechanga Elementary School, on the reservation, cultural resources protection, healthcare services, environmental protection, water infrastructure, senior support programs, youth programs, scholarships, energy infrastructure, and many more services.

And as many of you know, securing our right to conduct Class III gaming on our lands was no small feat. Collectively, we had to spend tens of millions of dollars in multiple ballot campaigns to simply confirm an inherent right. Central to that historic vote was our commitment to limit gaming to our tribal lands for the simple purpose of achieving self-sufficiency to our tribal communities. We thought then, as we do now, that this commitment was consistent with longstanding federal and state public policy of limiting gaming. Because of those precepts, tribes throughout California have entered into long-

term agreements with this state, have made financial commitments, and invested billions of dollars with the goal of developing world-class destination resorts on tribal land.

And indeed, the last time I testified before this committee was April 11th of 2007 when Pechanga sought ratification of our amended tribal-state compact. Those amendments included commitments by our tribe to significantly increase our base revenue sharing—for just 2,000 machines—from \$29 million to \$42.5 million—and that’s without adding an additional slot machine. That was just part of the agreement, the amended agreement.

This means, that without adding a single gaming device, we’ve increased our revenue sharing by 45 percent because, as the compact states, the payments specified in this subdivision, meaning the base payment and the payments for machines over 2000 games, have been negotiated between the parties as a reasonable contribution to be made annually in quarterly payments based upon the tribe’s market condition, its circumstances, and the rights afforded by this amendment. That’s a real key phrase describing the key of exclusivity that’s agreed to in our compact.

In our view, authorization of intrastate Internet poker would undo those precepts. My tribe would very seriously reconsider the revenue-sharing provisions of the amended compact because, clearly, the notion of people playing state-sanctioned Internet poker was not a market condition that was accounted for in our discussions. And, frankly, if this proposal had been discussed back when we were renegotiating the compact, our tribe likely would have rejected the amendment because, with Internet poker—and eventually Internet gaming, if you start adding Blackjack and other games—the gaming landscape and thus the market conditions would have been subject to rapid change and instability. From year to year, month to month, you wouldn’t know what the market would be or how to identify it.

So the question has been raised as to whether or not to authorize or whether or not authorization of intrastate Internet poker would constitute a violation of exclusivity provisions of the compact. Well, fortunately, I’m not an

attorney, but I do know enough tribal attorneys to know there will be no shortage of opinion on that issue. Unfortunately, this means the question would probably result in a protracted legal dispute that would necessitate resolution by the courts.

From a practical standpoint, and as a significant segment of the gaming industry, we are deeply concerned about protections for children and individuals that are vulnerable to problem gambling. How would the state keep children from betting online if we can't even keep them from visiting other illicit websites? How can we control the gaming habits of an individual in the privacy of his or her own home? We aren't the only ones concerned about protecting children and vulnerable citizens. The voters too are also reticent about the impact of intrastate Internet poker.

This past August, about five-and-a-half months ago, we, at Pechanga, decided to commission a statewide poll of 802 registered, high-propensity voters. Our purpose was simply to determine the voters' attitudes toward authorizing intrastate Internet poker because, at that point in time, we had seen no poll, no survey instrument, that attempted to objectively measure this so we went ahead and commissioned one.

We tried to make that available to you, Mr. Chairman, and to the Members of the Committee, so I trust that you have that poll as well as the interested-parties letter. Okay. Thank you. That's it, EMC.

You see, as we weigh these proposed policies that could significantly expand gaming, Pechanga believes we must take into account the opinions and concerns of the people of California, particularly in light of the commitments we have made about a limiting gaming. And those commitments came down to a promise that I actually made on camera many times through two statewide campaigns. Give us Indian gaming and we promise we're going to do certain things, like keep it on our own Indian lands. And the people agreed with that overwhelmingly—not once, but twice.

As we know all too well, there are two types of polls—the kind designed to elicit a particular and desired response and the kind that provides an

objective response. This poll is the latter; it's not the former. I believe we have made the actual top-line results also available to you so you can judge the merits for yourself.

I would, however, like to point out probably just a few of these sections to draw your attention to certain things. Let me point out, that without hearing any arguments either way, 61 percent of poll respondents reject the idea of legalizing Internet poker in California. That's out of the gate. Now of those 61 percent, 44 percent say they strongly oppose the idea. Only 36 percent oppose it—support it. Now after hearing arguments, both for and against, 61 percent continued to oppose with 46 percent saying they strongly oppose. So there is a slight bump on the no side.

Let me interject a couple other things about the public policy of gaming in California that was touched on by other panelists. Let me say this. Let us not confuse where exclusivity comes from. Yes, there are words explaining and identifying exclusivity in our tribal-state compacts. But exclusivity comes from the state constitution because of the support of the people of California. If we breach their trust, we risk breaching our exclusivity. What we have, we recognize that what we have is tribes here came through a vote of the people in California which amended the state's constitution, and the state's constitution is the highest expression of public policy in the state and so we take this very seriously.

Let me just move toward a closing here. Well, in a nutshell—I'll close with this idea—we recognize and we appreciate the state's urgent need to identify reliable sources of revenue. Question 20 in the poll deals with this. While it seems on the surface, especially in time of financial crisis, to look to gaming sources as an okay place to raise revenue, in the poll, 61 percent—no—69 percent—of voters, of respondents, think it's a bad idea. They think policymakers in the state should be focusing on making cuts, making hard choices, and doing other things, other than looking to gaming as an easy fix for raising revenue as a policy consideration.

Now our region, in Southwest Riverside County, is ground zero for the mortgage crisis. We see the effects of the recession every day, each and every day. Banks have closed. They've been seized by federal regulators. Signs—people upside down in their houses. The whole economy, the region, just really has changed. Pehcanga has also been affected by this downturn economically. And in 2008, for example, we had to lay off 300 employees. This was our first, and hopefully our last, layoff. We've tried to do other things. We've made numerous cuts to critical tribal programs.

Our ancestors' resilience instructs us that this too will pass and brighter days lay ahead for us and for the state, together. We are admonishing to not make a rash decision in these gloomy days. Let's not abandon the framework that has worked so well and served as a foundation for significant tribal commitments and our mutual tribal state agreement.

I'll be happy to entertain any questions. Thank you.

SENATOR WRIGHT: That concludes this panel. Are there any questions by the members on this panel?

Senator Padilla.

SENATOR PADILLA: Thank you, Mr. Chair.

I think after the last panel before the break, I pointed out two of the three questions I had coming into the hearing today, the first on the jurisdictional issues, since we're talking about the Internet here. There's always a debate whether we can or cannot control things that happen over the Internet, and I'm not saying there's a universal agreement, but the gentleman on the previous panel articulated how some people would argue that the state can do this.

Second, a question regarding exclusivity, and it's obviously a consistent theme throughout the day here. I think everybody on this panel was very articulate in their position, so that the third question, global question, that I really have is, for the chairman and chairwoman who are at the table now in opposition to the concept, I want to be clear that it's opposition to intrastate Internet poker, period, versus—is that a specific proposal or bill in front of us? But I think a lot of people are also responding to a rumored specific proposal. So there's a difference,

whether it's opposition based on exclusivity or for whatever other reason, to Internet poker or just specifically opposition to the way some people have suggested it or some people have interpreted it being suggestive. Obviously, Chairman Tucker and Chairman Martin have a slightly different position. Any response?

MR. MACARRO: Turn your mike on.

MS. LOHSE: Excuse me. Yes. So you're wanting to know if we're setting aside what this proposed out-there legislation is versus intrastate Internet poker, period; is that right?

SENATOR PADILLA: Is it opposition to gaming type under any...

MS. LOHSE: Absolutely.

SENATOR PADILLA: ...scenario?

MS. LOHSE: Absolutely, because it involves gaming devices, in our opinion, and what we have found, and it's obviously a threat to the exclusivity which ties in the exclusivity. So we believe that the intrastate Internet poker would include gaming devices.

MR. MACARRO: And agreeing with that, let me add that, you know, the introduction of this idea or the concept as it's been put out there so far, we are in opposition of that and others like that. So it's specific. Yes, we're in opposition to that and even broader things because of the exclusivity issue. It is a game changer. It's an unknown variable. You know, there's enough variables out there for us to try to control for.

You know, for instance, the competition factor between tribal casinos—it's fun; it's healthy. You know, it is what it is. We don't have a choice in terms of where our land base—that was determined for us, you know. Where our tribal homelands sit today are where our casinos are. So each tried to make the best of a demographic that surrounds us or maybe not. Maybe one that's 60 or 100 miles a way or right next to us, it is what it is.

This is a game changer, this proposal. There's no way to—there's no way to know. Is it a short, big wave? Is it a big, long 20-year wave? What we do know is that we tried to protect and insulate from these very things for a defined period of time through our tribal-state compacts, and this has the look and the feel of

something that would breach exclusivity in that compact. And what we're saying is that, you know, the deals we have are 30-year deals; and this year, there are 20 years left on this deal. So maybe in another 20 years, we can talk about the impacts of this if there are no more exclusivity provisions.

Just as a personal note, I don't ascribe to the notion that there is an inevitability of the doors being blown open on gaming statewide. I've watched the polling for the last ten years. You know, we did two large-state propositions, ballot propositions, Prop 5 and then 1A, really close to each other, and then we monitored public sentiment, voter sentiment, I should say, not just public sentiment, high-propensity voter sentiment in particular since then, and I can tell you that the proponents of this particular proposal are out of sync with what high-propensity voters in this state are feeling and what they're expressing.

MS. LOHSE: Could I just add one other thing? And this is not speaking on behalf of CTBA but, rather, as our tribe. Chairman Martin had indicated that, you know, they started very small and had grown over the past 25 years. Well, and that's been kind of a story for a lot of the tribes, except for we're located in Tehama County, in the north part of the state. We're not in Palm Springs, Southern California, anywhere near anything that's large. And our employee basis is 500 people. And in a state that's fifth, you know, highest unemployment in the nation, you know, it does possibly have an impact upon us, employee-wise, if we start losing business and, you know, we—that's rough during a time. I know the state has enough on their shoulders without possibly seeing more people, you know, go by the wayside and get into the lines of unemployment.

So, you know, there are those, all those impacts or something that I think again can be looked at as an exclusivity issue, as a gaming-device issue. These are asides but they're important to consider as you're looking at the whole issue.

SENATOR PADILLA: Mr. Chair, my purpose in asking the question is, I'm not suggesting any of the panelists right now said in their comments or in any of the letters that your names are a part of in our packets—but in reading the materials that were supplied to us, some of the letters just said no Internet poker, period. Others were a little bit more specific in saying, you know, we don't think a single tribe and a couple card clubs ought to have, you know, sort of a monopoly,

et cetera, which, if you really want to read between the lines there, could suggest an opening maybe if there was other arrangements or multiple participants or different parties. So that's why I wanted to ask the question, Are you opposed to it, period—which is what I'm hearing, for those of you who testifying in opposition—versus just the rumored proposal? And again, I expect Chairman Martin has a different position than others at the table and Chairman Tucker somewhere in the middle.

Thank you, Mr. Chair.

SENATOR WRIGHT: Let me, I guess look at a couple of things, and what I hope we hear is, again, we're not looking per se at one of the propositions. The concern I have is, that irrespective of whether or not California adopts an Internet poker policy, that doesn't mean that people aren't going to do it. I mean, as I looked at some of the other countries that are currently involved, when Sweden enacted their statute, they were only successful at capturing about a third of what was already taking place. So if we enacted a statute in California, for example, I'm not certain that we would actually create a new Internet poker player. What we would do is capture some of the revenue that's already leaving.

Now there's an unknown. That unknown becomes, Did we take someone who might have gone to the Pechanga Casino and had them play at home? Answer, I'm not sure. Did we take someone who might have gone to Tehama County and had them play at home? Answer, I'm not sure. If we don't do anything, will people continue to play Internet poker? Absolutely, that, I am sure. And will they play more? Yes, of that I am sure. And if we watch, we'll continue to watch those dollars get away from us. And I'm not sure that the risk to both the state and your business is necessarily served by doing nothing. I'm not sure what we ought to do, as I'm sitting here right now, but it's not as though we're sitting here making a decision as to whether or not people are going to play Internet poker. That ship sailed. So the question becomes, I think, for all of us is, Do we get in the game and try to get a piece of the revenue that's already moving, or do we watch those dollars leave? Because it's not like the decision here is to either authorize or make it work. The issue of exclusivity—and again, we are not going to

resolve it here because I'm not a lawyer either. I'm just a poor kid from South Central Los Angeles—we would say a hood rat in my neighborhood.

But we're not going to resolve the legal issues here but, you know, but the concern I have is that—I mean, you know, at any given point, there are probably, at this time of day, I'm going to guess that there are 30,000, 40,000 people right now playing Internet poker in California. We don't get a dime; you don't get a dime. As that number grows, there's a bigger piece that we simply don't get. I'm not as wedded to a proposal as much as I am the fact that we're looking at money leave. I mean, you know, in that context, you know, Members of the Panel, I mean, we're having serious discussions about legalizing marijuana. Same drill. I mean, we can pretend people ain't smoking it, and there are arguments as to the good and bad of whether or not you should or you shouldn't. Is it medicinal; does it help glaucoma? As a glaucoma patient myself, I'm looking for—I mean, but (laughter), hey, I take drops twice a day because I've got glaucoma. If I could substitute out—but anyway (laughter), all I'm saying, in all seriousness—I'm sorry—what I hope we'll be able to do is look at the concept notwithstanding the proposals but just say—I'm now going to rephrase Senator Padilla's question: Should we do nothing?

MR. MACARRO: The answer is yes, probably, from a legal standpoint. I'm not sure you can do anything, in terms of the exclusivity argument. You might be prohibited from doing something, unless you willfully decide and do some cost benefit, if it's going to benefit the state greater to pursue this path of intrastate Internet poker versus honoring agreements of tribes over the next 20 years. It's that simple. You might have bullet-proof systems for intrastate Internet poker. Heck, the federal government might—Congress, I mean—might pass a law that allows California to opt in and a lot of the public policy discussion might go away. You know, software geniuses might come up with this stuff that will, you know, 100 percent keep minors off the Internet; you know, credit card abuse and gambling addicts will be weeded out through all the software, stuff we've already heard; the best systems will be in place. And I'm suggesting that it still may not be possible legally because of the exclusivity arrangements that the state made with tribes.

SENATOR WRIGHT: Right.

MR. MACARRO: Now if that's not a big enough reason, though, to keep the state from moving forward, I don't know what is because there's been, you know, agreements that the state has broken with tribes in the past where agreements haven't been honored by both the state and the federal government.

As far as, you know, doing nothing, meanwhile everybody's making hay, you know, there's fish to be caught in the ocean right now but I'm not on the boat out there to catch them, and neither are you. So, you know, they're not being caught, you know, so we're not fishing. I don't know. What does that mean?

The argument that the status quo already allows this to happen, and we're losing out because we're not there, that's neither here nor there. You know, it's not a good public policy argument and that's not something that works for me either. So, you know, let's focus on the things that are really important here, like exclusivity.

SENATOR WRIGHT: Okay. But I think, well, again, Mr. Chairman, we're not going to resolve exclusivity today because neither one of us are lawyers. Leg Counsel tells me that it doesn't violate exclusivity. I've had lawyers tell me that it does. So now I have something that's really unique in America. I've got lawyers who don't agree. (Laughter) And it might well be, that should we decide to proceed, that one of the things that would certainly happen first if it was up to me, is that the issue of exclusivity would be resolved in a court because clearly it would be a business that you couldn't embark on. If there was—in real estate, we would call that clouded title, so that issue would be fully resolved prior to the state engaging in any activity.

But unlike the case of fishing, if I were to take that analogy, the concern I have here is that there are dollars leaving here at a rapid rate. And those dollars are leaving irrespective of what we do. One could argue that the current status of Internet poker also violates exclusivity because, frankly, the same people are already playing. See, I'm not sure, that if we did this, that we would create a new player. So if the people are already playing Internet poker, the only thing we're talking about at this point is whether or not the state gets a cut. It's not a

question of, Are they going to play? They are. That ship sailed. Not only are they already playing, but the number of people playing is allegedly growing.

We'll hear in one of the later panels that represents player associations that we probably represent in California a sizeable percentage of the world's Internet poker players. The only thing that currently exists is we don't get any. So I mean, if I—we could argue now—you could argue now—and I don't necessarily want to put ideas on this—but you might want to go to court now and say that the current situation violates exclusivity because the thousands and tens of thousands of people who already play, albeit not state sanctioned—but as you may have heard for the attorney general...

MS. LOHSE: I believe that would be the difference, is the fact that it is not state sanctioned, and so we can't control something outside of our agreement, so our agreement with you is state sanctioned and that's our compact. So that's where we draw...

SENATOR WRIGHT: The line.

MS. LOHSE: ...the line, as far as what is pertinent to us and what affects us.

SENATOR WRIGHT: And under current, under the current status we have from the attorney general, it's not even clear today that those people who are playing Internet poker are even breaking the law. I mean, we might have the ability to challenge the money, as you heard that they did in Washington State. I mean, they have, you know, gone to the virtual cages and taken, in effect, cash from the people who did the chips. But I'll bet you, I mean, as already happened, for example, in one case that I'm aware of, where the people in the Isle of Man reimbursed all of the people who had their winnings confiscated, plus, interest, and then gave them new accounts that were also offshore so that the IRS couldn't get them again.

So I'm just saying, there was something like \$300 or \$400 million—I forgot the exact dollar amount—but one of the poker sites reimbursed all the players who had their monies taken, paid them interest on what was taken, and then gave them new accounts offshore that the IRS couldn't touch, and they kept on trucking. So I'm just saying, you know, Washington got that \$200 and whatever

million it was one time and they ain't going to get it again, and I'll bet that those people were made whole by the sites because the volume of dollars that you're playing with becomes so large that it morphs.

And it's not clear—I can't tell you today that we have a solution that would necessarily capture that because the sites that we created, if we did, may not be as attractive as—and again, you'll hear in one of the later panels—they may not be as attractive as the loyalty that the players have to the existing sites and we still may not get the money even if we set it up. But I hope that we're looking at the big picture.

Again, I'm not necessarily a fan that the state itself look forward to making its revenue in gambling. That would be, you know, my personal view—and I can't even play poker, so it's not like—I'm trying to learn, though—I am trying to—but I hope that we look at the broad scale—and in this one, understanding that people are doing this in California as we're sitting here and, again, not to give you a legal avenue, but one could say that exclusivity is being violated right now, given the fact that we're not prosecuting people who are playing. We know that it's being done and a lot of money is escaping from any form of taxation.

I'll go right back because I kept talking and I over-talked Senator Yee, but keep your question and come back, sir.

SENATOR YEE: Thank you very much, Mr. Chair.

I want to just articulate my position and it's probably not all that different from what the chair just simply mentioned. I don't think the state of California is interested in getting into a battle with sovereign nations. I think a contract is a contract and an agreement is an agreement. But there are times when we are in extraordinary situations where we do need to kind of look at other avenues to generate revenues.

We have a—I think in the last budget session, we cut \$42 billion. We're looking at another \$20 billion plus. There's some in the capital that are thinking about maybe drilling oil offshore, you know, unheard of, but still being talked about. So I think we are in rather extraordinary times, and so the question then becomes one of, Are there other revenue sources that are out there? Now I don't gamble; I don't play any of that, but I go to a card club in my area, Lucky Chances,

and half my relatives are there, you know. And so I know they are playing and I know in talking to them that they are also playing on the Internet, and that is revenue, I think, as the chair said, that we don't see at all; we don't get at all. And so if it is happening already, then it seems to me, that if we are prudent and that we are trying to take care of the issues at hand, which is this horrendous deficit and the cuts that we are making, that we've got to go out there and find a way to generate some additional revenue. So this is revenue that is out there and we are not capturing. And I don't think that anybody is going to rush into this without some consideration about what is the effect it's going to have on you all.

Now I think there was an early panel that said that, you know, the market share of gamblers are discreet from what you take and what may be those individuals who are involved in Internet gambling. Maybe it was a cursory comment. You know, maybe we need to look at it a little bit more. But if they're discreet, you know, I don't know how it's going to financially affect you. Then I think, if it's not going to financially affect you, or maybe it may minimally, but if it's not going to do that, then the issue really is about exclusivity. And if it's about exclusivity, then it seems that that is something that's been discussed and negotiated. And as nation to nation, you can't somehow turn your eyes blind to the fact that we're cutting education; we are cutting childcare; we are cutting healthcare. And if you are a nation of leaders and you are leaders of your people, you can't tell us that while we are turning kids away from childcare and public education, that you can say, well, I'm sorry; that's just the way it is.

So we've got—I've got a responsibility of finding what additional resources there might be for those children and those poor people. So that's, I think, where I'm coming from. I think that we need to have some more discussion about how do we proceed, but I don't think you can close that door because we've got a job to do, and that is, to take care of the people of California.

And so that's where I'm at, Mr. Chair, and, you know, I'm going to be supportive of, you know, trying to find, you know, where and how we're going to be able to move this forward.

MS. LOHSE: Oh, I'm sorry.

SENATOR WRIGHT: I think you were up, sir.

MR. MACARRO: I just want to say, these are extraordinary times, and I don't think the people of California would appreciate a do-nothing approach to any type of public policy issue, and the California Association of Tribal Governments would like to see some type of independent study being done. I know we've been monitoring these situations for the last six or eight months, and the questions of exclusivity, the estimates on the revenues, the poll numbers, all those things, seem to change, depending on who you're talking to, and so a recommendation that we would have is some type of independent study be done so that we can move forward. And if we decide in the end to bypass it, then we can. But I certainly think something needs to be done to move this in the right direction.

SENATOR WRIGHT: Yes.

MS. LOHSE: Yeah, it's not a good environment to do nothing, obviously. But again, whether the poll numbers change, opinions change, those kinds of things, what California Tribal Business Alliance stand by firmly is that our compact language does not change in our understanding in regard to exclusivity and what it would cost the state. If those payments stopped, how it would affect, as you were saying, to the people that are in need, he's a representative of many—Mr. Clarke is representing several tribes that depend on that revenue-sharing trust fund. So if that stops, that affects hundreds and thousands of tribal members and their healthcare and their education and their housing, those kinds of things.

So, you know, I think we're walking down a road that, you know, it's like, you know, you're robbing-Peter-to-pay-Paul type of thing. You're right. It is undetermined. We do know, again, people are playing it, but we don't have the information as to what really is the, you know, the amount of money that we could glean from that for the state. But as I suggested, the card rooms grossed \$889 million last year and only paid for state regulation—10 percent of that, \$89 million a year.

So, you know, let's look at things that we have numbers on. We don't have numbers on what, how many Californians specifically are playing, how much are they betting, those kinds of things. We do have those reported numbers. There is something that you can probably tax.

SENATOR WRIGHT: We do know that the card clubs pay income tax and they pay business licenses in the jurisdictions where they operate.

MS. LOHSE: For state regulation. We're talking money that's going straight to the General Fund.

SENATOR WRIGHT: They're state income tax that they pay.

MS. LOHSE: Which our money is.

SENATOR WRIGHT: That's what I'm saying, but the card club pays state income tax. He pays local business licenses and he pays for the regulation.

MS. LOHSE: Our employees pay state income tax.

SENATOR WRIGHT: As do everybody.

MR. LOHSE: They pay federal income tax so...

SENATOR WRIGHT: As do everybody.

MS. LOHSE: Exactly.

SENATOR WRIGHT: So...

MS. LOHSE: And that's exactly it. But if you're looking at revenues, that's a defined number. You want a percentage of something, that's a defined number rather than trying to figure out how much could we possibly get from however many Californians are out there. So I'm just saying, when you're looking and considering information, the fact is, we would say it was an exclusivity breach. That's \$365 million off the table.

SENATOR WRIGHT: And again, to, not to beat a dead horse, so to speak, before a proposal left the legislature, a judge would determine whether or not it was exclusivity. So I couldn't do that. Leg Counsel could render an opinion, as they have, and they said that it wasn't. Would I rely on a Leg Counsel opinion, frankly? No. What I would do is, we would go to court with a piece of legislation in hand, and a judge would tell us that because you're absolutely right. If it turned out that we were going to engage in a proposal from which you would have to subtract the money that you have from the money that you hope you get—I mean, in a game of Let's Make a Deal, you know, it's kind of like, Do I go for this in exchange for what's behind Door Number 2? But I have no idea what's behind Door Number 2, but I do know exactly what this money that I'm currently receiving is.

You make absolutely the right point. And before we would go down that path, we would clearly identify what Door Number 2 is. So I can assure you that we would not just assume that there is no violation of exclusivity so there's—I don't know that there's anyone on this panel who just says, I absolutely know what the answer is. I don't. I've heard Mr. Foreman. But again, I mean, Lord knows I've heard lawyers disagree a whole bunch of times. I mean, I've got lawyers that I'm talking to right now that disagree about something that sounds as simple, but another discussion. But clearly, lawyers disagree all the time.

MS. LOHSE: It's kind of like tribes.

SENATOR WRIGHT: No.

MS. LOHSE: Don't ever assume.

SENATOR WRIGHT: No.

MS. LOHSE: You've seen one; you've seen 'em all. (Laughter)

SENATOR WRIGHT: But I'm just saying, so the issue of that would clearly have to be resolved before we did anything because you're right. I mean, up to and including whether it be meet and confer, or it might mean that we, you know, somewhere a meeting conferred. Maybe you go back and renegotiate some element of the compact itself. Or, again, it clearly depends on what the outcome of what a judge might say, and I'm not quite, I'm not sure exactly what would take place at that point.

MS. LOHSE: I agree. I just felt it was our responsibility to bring to you the issues that we receive that would follow if we continue on down the road to entertain the idea of intrastate Internet gaming, whatever the agreement may be.

SENATOR WRIGHT: So I guarantee we'd be in court.

MR. MACARRO: Mr. Chairman, let me just finish up on one point here. When times are good, the state has an agreement with tribes. When times are bad, the state can break their agreement with tribes because they have to look for extraordinary means to raise revenue. That's a dangerous road to go down.

Now what I heard you just finished saying right now, though, sounds more like—well, it is in the camp of honoring the agreements that the state made. Nothing would move unless and until a judge gave an opinion and we knew—we

would know if a proposal was either going to violate or I think not violate, nothing would move. So you would wait until a judge gave that kind of blessing or opinion.

SENATOR WRIGHT: Right. I mean, in the utility business where I spent a great deal of time, you can't sell bonds, for example, if there are issues relative to the legal revenue that you're going to repay the bond with. I mean, we would be hard-pressed to either issue a license or anything else if there was a legal question as to whether or not, what we were trying to sell may not be legal.

So you're right. I mean, we would have to resolve that unequivocally before we could even go to the market, whether it would be a monopoly system or a licensing system or whatever we had. And if it turned out, Mr. Chairman, that it was determined that it did violate exclusivity, then we would probably be back in another negotiation of meet and confer to determine, if it's exclusive, then we have to renegotiate that portion of the compact pursuant to—what is this section?—2.6 of the compact language.

I mean, I'm clear that it's not like we can just say, oh, you know what? We're the good folk and we can just do what we want. I think that that ship has sailed. And unlike in years past, I suspect that the Indians probably have a lawyer or two that they can call. So, you know, this ain't like the days when they bought, you know, Manhattan for some beads and stuff so...

MR. MACARRO: At least we're going to say something this time, and we have a thing or two to say about...

SENATOR WRIGHT: No. I think so.

MS. LOHSE: And I wore as little jewelry as possible. (Laughter) I didn't want you to get any ideas.

SENATOR WRIGHT: And I think that that becomes important, that we would—I mean, this is not an attempt to say, oh, no, we just think we're going to roll you because it's Tuesday and we can get away with it—not by a long shot—and we will fully recognize that. And I mean, not at the point of being redundant, I wish I could say, you know what? I just read this section of gaming device—I don't know. And it might be that that's where we end, where we end up again. When I looked at what Leg Counsel wrote, for example, Leg Counsel took off on some

tangents that weren't contained in what this was to the point where I go, Where the hell did they get that from?

Here, we invited earlier the Gaming Control Commission and they said, you know what? We don't even want to come sit down because we don't even have a position yet. So there is still a whole lot of time left on this clock, so I don't want anybody to think that this was kind of a shortcut to try to say, you know, we're going to cut and run.

I mean, and as far as revenue was concerned, the other thing I would want to make clear is that, even if we were able to do this today, we ain't going to see no money for two or three years. I mean, we will have resolved our current financial situation long since—they will park that guillotine out in front and we'll be gone before we really see—I mean, you know from your own building of businesses, as you've done, it ain't like we're going to see money from this by the summer if we did it today. So we still got a lot of time left on the clock. If we did it, we'd still have to build the business, and we would still have to convince people who are already playing over here that they really want to play over here. And as I've seen from Sweden, as I've seen in Italy, as I've seen in other places, that too is more than a notion.

And Mr. Martin, I think you had your hand up or...

(Inaudible Comments)

MR. MARTIN: Mr. Chairman, under Article IV, section 19(e) of the California Constitution, the legislature does not have the power to breach exclusivity because, in order to breach exclusivity, the legislature would have to be authorizing either a gaming device or a bank or a percentage gain. And in *Here ?? v. Davis*, the State Supreme Court said, those are indicia of the casinos currently operating in Nevada and New Jersey. And Article IV, section 19(e) of the Constitution says, the legislature may not authorize and shall prohibit casinos of the type currently operating in Nevada and New Jersey. Thus, were the legislature to enact the statute that violated exclusivity, that statute would be unconstitutional, ineffective, and thus exclusivity would remain intact. So you're absolutely right. It ends up in court with the judge making the call.

SENATOR WRIGHT: Right, and we would do that. But again, I don't think, at the risk of speaking for the members of the panel, I don't think that there's anyone here who would knowingly set out to say that they're attempting to violate exclusivity. So that's not the question before us. If we were moving towards something, again, we would have to resolve those questions as best we could and it would clearly be a condition that, you know, again, if it went to court, that that would be the pact that we would follow. I mean, so this isn't a jail breaker by any means, and we're not—as you've looked at this agenda, we're not looking at any specific elements of a proposal which is why, again, when we brought people from halfway around the world, so it wasn't just we wanted to have kind of like an interstate squabble. We were looking at all the options that we could look at as we looked at this issue.

I mean, frankly, there weren't many people in California six months ago who knew very much about this at all. We probably have enlightened a few today, and there's still a great deal of work yet to be done because I think the chairwoman from the Tribal Business Alliance—and I don't want to just use your first name...

MS. LOHSE: That's all right. It's Leslie.

SENATOR WRIGHT: But just as she pointed out, you know, there are a whole lot of unknowns that we don't yet know. And probably one of the worst things you can do in business is, if you're trying to place a value on something that you want to ___ license or sell or do whatever with, if you don't know what the value is, it also makes it difficult for you to place a value on it, which gets to the next point of—you may have seen in the earlier discussion, Senator Harman and I were asking, in the Italian model, how they decided to even price it, X number of dollars over five years. Do you tax the pots? One of the things we know, for example, is if the tax on the pots is too high, then it discourages the people from even wanting to play. I mean, that's one of the knocks on our current lottery system, is that the price pool is too small to make people want to play. I mean, all of those become considerations that we would have to look at.

I'm sorry. Chairman Martin, I kept running my mouth and you had your hand up.

MR. MARTIN: I was listening.

Chairman Macarro spoke earlier about the 5 percent of the time that Morongo and Pechanga may disagree. Probably this is one of the very few times that we don't agree on other things. And this exclusivity seems to be the issue at hand today. Our legal counsel feels that there is no breach of exclusivities. And when this opportunity came to the tribal council, we looked at it. We wanted to make sure there was no breach of exclusivity; there was no sovereign rights that were going to be, have a problem with. And in today's business world, when we're losing market share, we're going to look at all things. As long as it's not illegal and the tribe can—it's not going to hurt anybody. We're going to look at these, any deal that comes across the table, and this happens to be one of those, and we want to be out on front on this. It's gaming; we feel we have the expertise in gaming; so we're not going to sit back and let all those dollars leave this state. We feel that those dollars should stay here in this state and we feel that the state should tax them. The state should get its fair share off all those billions of dollars leaving. I wanted to get that clearly said.

SENATOR WRIGHT: And that's fine, and I want to make sure that there's no one else on the panel who has a question. And, sir, that's fine, and as I said, we weren't doing a referendum per se on what you brought because I can tell you that the final product might not be what you brought. Again, that's why I don't anybody to think, wow, we're coming to actually do a hearing on the proposal that came forth from one of the particular tribes, not the case. And I want to make clear, that from the standpoint of the chair, the property, the value that we're discussing, belongs to the state of California. It doesn't belong to the card clubs, nor does it belong to one of the particular tribes. It is an asset, per se, that would be an asset of the state of California.

The job of this committee and, ultimately, the legislature, would be, How do we best get the value from this potential asset? Is it the way that it was proposed? I don't know. Is there another way? I don't know. But I want to make clear that it's not a case where it's your proposal versus nothing. At this point, I think, as Senator Padilla raised, we're talking about the global idea of Internet poker. How that asset is valued and how the asset is marketed, that kind of, sort of, becomes another discussion. And that's not to say that any particular idea has been

discounted or discarded. It's just to say, that as I look at it, the state potentially has an asset that is currently underperforming. Do we have an obligation to take this underperforming asset and try to turn it into a performing asset, notwithstanding the issues relative to exclusivity? If that becomes an issue, then it really doesn't become an underperforming asset any longer because, as you attract the revenue that you get from what you think you might get, then you start from a whole which then changes the equation of how you value the asset. I mean, that's a lot of gobbledygook that comes from somebody who's the utility regulator. But at the end of the day, you market and value an asset based on something.

Mister—you had your hand up, sir, and I kept going on.

MR. TUCKER: I just want to make clear to you, and I want to thank you again, Mr. Chairman, that I'll take this back to CNIGA because it is an organization in California that's for gaming for tribes, and all the information we got today has been tremendous. So I will take it back to that organization and we'll come up with something. But hearing all this today is very, very enlightening to all the tribes in this state, so we will make sure that gets out as well because it is huge; it's a huge situation and everything makes a lot of sense. But, you know, I want to promise you—I want to thank you and promise you—that this was going to happen on behalf of the organization. Thank you.

SENATOR WRIGHT: You get the last word. I'm sorry.

MS. LOHSE: Thank you very much. I just want to say again, thank you for allowing us to come here and share what our understanding is and what our concerns are and to remind you that we are Californians too, so we are in this with you all the way, as far as dealing with the economy, education, and the general welfare of California because we don't get to become an LLC or some other company in another country, another state. We are here. This is where we are from. These are our lands that we are living on.

And as far as litigation goes, hopefully we don't have to go down that road. And as far as depending on perhaps the state's interpretation of the compact, I think Mr. Foreman kind of knows that sometimes they can be wrong because right

now I think we have a few more licenses out there than was previously perceived. So just with that thought, thank you.

SENATOR WRIGHT: Thank you all so much.

Any other questions for the panel?

Again, thank you all for coming. I know that this was kind of a pain to get here and people have stayed overnight. Appreciate your testimony. We've got those things in writing. If there's some other information that you'd like us to have—we've got the polling information and the other things—if you'd please get it to the committee, we'll make sure it's a part of the record. Thank you again.

Okay. We're now going to call up the card club.

Leo Chu, Keith Sharp.

I thank both of you for coming out today. Mr. Chu, I'm going to take the home court advantage, and Mr. Chu represents Hollywood Park in the great city of Inglewood. And giving deference to home-court advantage, Mr. Chu, welcome to...

MR. LEO CHU: Thank you.

SENATOR WRIGHT: ...Senate G.O. Committee.

MR. CHU: Thank you. Thank you very much;

Actually, this is the first time I've ever done any testimony at a public hearing, so I'm a little nervous. However, Chairman Wright and Members of the Senate G.O. Committee, as a matter of fact, it took, me two weeks to prepare my speech. But I think after hearing all the testimony and everything, I'm going to throw this out the window because everything I want to say actually has been covered.

However, I shall introduce myself. My name is Leo Chu. I'm the owner of the Hollywood—actually, my wife is the owner of the Hollywood Park Casino. I work for her. In Los Angeles, I'm partner in Crystal Casino in Compton and also Lucky Derby in Citrus Heights. I'm also a former California Gambling Control Commission Advisory Board member, and I also served on the Board of the California Problem Gambling Council for 12 years. I'm also a board member of the CGA, which is the California Gaming Association which comprises of over 90 car clubs up and down the state.

And I want to thank you, Chairman and the Committee, to give me the opportunity to let me speak on behalf of the card clubs about the Internet poker.

The main topics of this actually now is basically revolves this exclusivity. But I think in basics is put that aside. These are the issues: How can we regulate it? I think Mr. Appelsmith said it very well this morning what he can do. Can we guarantee a revenue from it? I think there's absolutely revenue from it because, even from this study that they say they're going to lose \$350 million, if you put the contributions from the tribal casinos to the state away, it's almost \$400 million revenue being generated.

How could it be operated? I think the only approved, state-approved, or city-approved poker places are really the card clubs and the tribal casinos. These are the two legal entities that's approved that can play poker, and we have a lot of experience in the past. Well, regulated poker clubs has over a history of 100 years. We actually have a card club up north, up north in Pechanga, is over 100 years old. So we have a track record and deregulated ??, comply with the law, and do the things that we should do according to the law.

All the other areas actually has been covered quite extensively. And I think the other things obviously, either we will preempt the federal bill that's coming out this year, the Frank bill, also the other bill, and it might put us in the backward position and we in California need to think about what are going to do for us in California.

Online poker actually presently generates about \$256 million from the illegal gambling sites, if not more. I believe the revenue will be double or triple if we can make this legitimate, meaning, that people will only want, always want to play on the legal approved sites, especially on gambling.

I'll give you an instant that this website, this actually is a, this CEO was arrested in Dallas, when he was arrested, that he had to stop taking bets. He actually closed the website right away, and he owed the players \$16 million, just walk away, just walk away. So I think this is a very, very important point that we need to regulate this business.

Now let me give you a little example. About 16 million poker players in California plays every day, that plays every day. Do when the bill was signed, the

UIGEA bill was signed, I thought, I thought this might be a terrific idea. If they don't take bets in California, maybe I can have an electronic poker table in my casino and I can get those people that play at home come out to my casino to play. So I spent some money to invest some money and actually built a little electronic poker table pit, tried to get those Internet players out from their homes to come to my casino to play. And you know what? I didn't get any business from that. They did not want to come. They only—they still play at home. They don't want to dress up and then come to any of the casino to play or to any poker card clubs to play.

So these people, whatever we do, they'll be playing online. So what this regulation would do actually is going to be in fact to get those 16 million people to pay to the operators, that the operator will pay taxes to California. So I want to use the Las Vegas slogan which is, Whatever happens in California should stay in California.

I think that most of the things has really been covered. I don't want to be redundant about repeating any of those other points. I think today, today I learned a lot. Today, I think today's experience to give me a better experience than my 15 years in the gaming business. And today, I learned from all the sides, even from Sweden, Italy, by giving us the—I researched on the Internet gambling for the last eight years, and so I know quite a bit about what they do on Internet and so forth. And I always wonder, I always wonder, what is going to happen, what is going to happen, on how we can regulate Internet, things that happen on Internet. So I think this is the first step that we should obviously—we have to take care of the other legal issues, but I think this is—if the state decides that this is actually a good thing to do, which I think definitely is a good thing to do—that the tribal casinos and card clubs are the best ones actually to be on the first hand to help, how we can regulate and how we can do upgrades in strict accordance to the law because we've been doing this for a long, long time, a long, long time, and we have the identity; we have the knowledge; technology, there's no problem, as was testified earlier in the morning. What we do, what we do here, actually the division of gambling knows all of us. We are all under the jurisdiction of cities, county, and state. We are more regulated than anybody else. We're worse than a bank.

We're under Title 31, and yet we have to comply with the laws of the state, the county, and the local PD from the cities.

So we know how to do it, and I think that's why, if this thing happens, we are the best choices actually to be able to do this venture. Actually, I did not follow any of my speech that took me two weeks to write. But anyway...

SENATOR WRIGHT: But we have your comments. If anybody would like to read them, they'll be a part of the record.

Mr. Sharp, if you will go ahead again. We'll do questions to this panel at the end as well.

MR. KEITH A. SHARP: Thank you very much, Mr. Chairman and Committee Members. Again, thank you for the opportunity provided me to testify today before you.

My name is Keith Sharp. I serve as general counsel to Hawaiian Gardens Casino, and the Normandie Casino, and several other card rooms throughout California. I have advised the card room industry for close to three decades on matters concerning regulation, compliance, operations, and management.

You are here today to determine if online poker is a good bet for California. The fact of the matter is, though, however, that Californians are already at the table but the state isn't in the action as of yet.

As a *Sacramento Bee* editorial page opinion by Internet legal specialist Martin Owen recently stated, there is no policy gamble for the state. Internet gambling is already a fact of life here. California has been licensing horseracing bets through Internet services, such as YouBet and TVG for years.

Twenty-nine states use the Internet to help horse betting today, and five more use it to sell state lottery tickets. Internet gambling is an industry that started at zero not too long ago and is now predicted to gross close to \$25 billion in 2010.

A licensed online poker network is the best protection that the state can offer to the young, the vulnerable, and the problem gamblers who are already being reached by the offshore sites.

The card room industry in California has evolved from the days of the Wild West with no regulation whatsoever into a sophisticated, highly regulated industry

which provides thousands of jobs and significant revenues to California and to local communities. I have seen this evolution firsthand over my 27-year tenure in the industry--beginning with the Gaming Registration Act, the passage by this legislature of the Gambling Control Act in 1998, which introduced a tremendously comprehensive licensing and regulatory framework, to present day with the implementation of Minimum Internal Control standards that govern in detail all aspects of card room operations. This legislature has made clear its unwavering interest in appropriately regulating the industry, and the regulators have been and are diligently carrying out that task.

California houses the largest poker rooms in the world. We, along with the gaming tribes, are *the* only groups to whom the state of California has entrusted the lawful play of poker. We are fully licensed, having undergone a licensure and backgrounding process which I advise my clients is more comprehensive and rigorous than that required for a federal top-secret clearance.

Several earlier speakers have emphasized ensuring that operators are honest and have integrity is essential to the process. As per the specific requirements of section 19857 of the Gambling Control Act, our licensure as card rooms means that the state has found us to be persons of good character, honesty, and integrity. We are known to be compliant with and expert in underage exclusion requirements, patron self-exclusion, and problem gambling assistance, and Title 31 currency reporting requirements.

California is now in a prime position if it chooses to leverage it. With California's card rooms and tribal gaming, the licensing and supervision are already in place and can be readily and easily and quickly adapted for intrastate online poker so that consumers can be protected, jobs created, and state revenues realized at the earliest possible time.

The regulation of gaming has always been and should remain a matter of state's rights. You have heard and will continue to hear of the threat posed by pending federal legislation to California's efforts to appropriately regulate and capture revenues from Internet poker. The card room industry is mindful of these threats and views them as very real and very imminent. California needs to be ahead of the curve.

We respectfully suggest that the time for the legislature to act is now. Consistent with its history of closely and comprehensively regulating gaming and fostering consumer protection, the state should act quickly and decisively. It should do everything possible to ensure that Internet poker is conducted openly, honestly, and with the appropriate protections in place to prevent underage participation and provide problem gambling assistance.

The establishment of an alliance between all tribes, gaming and non-gaming, all card rooms, and the state provides important certainty that Internet poker will be conducted by poker experts to whom the state has historically entrusted the play of poker—experts who are well known to and located within California; who have a proven track record of adhering to and being successful within a comprehensive gaming regulatory environment in California; and who will be highly motivated to ensure that the regulatory scheme is strictly adhered to, lest not only their Internet business but their brick-and-mortar operations in California would otherwise be jeopardized. In poker vernacular, the card rooms will be all in. Others who do not have our expertise and who are not invested in California simply cannot provide California and its citizens the same assurances.

The state and card rooms have enjoyed a positive relationship for many years. We seek to continue and expand that partnership together with the tribes as we address the ever-increasing presence of the Internet and define its role in our businesses and our lives. We believe this partnership provides the state with the greatest opportunity for success in capturing and keeping Internet poker dollars in California where they belong.

In sum, legalizing and licensing Internet poker for California makes sense. And doing so with California partners you know well and have long counted on to ensure public safety and gaming integrity is essential. Thank you.

SENATOR WRIGHT: Thank you.

I want to do something as just a topical question that's kind of a holdover from the last panel.

As a card club in California, what revenues do you currently pay? I mean, there was a bit of confusion, and I want to just get that on the record. How are you taxed, regulated, and what do we get from the card club that you operate?

MR. CHU: Card clubs in California, basically our license is issued by the individual cities. So usually what we do in the Southern California card clubs, we pay the city a specific gaming tax, anywhere between 10 to 13 percent on gross revenue. And also we pay the state—and also we pay the state—I believe that we pay a table fee. Table fees is graduated from, if we have one table all the way up to over, I think it's 44 tables. So it's a graduated fee. The more tables you have, the higher fee that you pay. So these are the two fees basically we pay—the city—one to the city and one to the state.

SENATOR WRIGHT: And as a business in California, you still pay income tax on your profits?

MR. CHU: Just like a regular corporation, yes.

SENATOR WRIGHT: I just wanted to make that clear because there was a perception that you somehow skate on contributing to the state economy and it just comes in, in a different way.

Senator Price.

SENATOR PRICE: Thank you for comments from both.

I remember late last session, we were told there was some urgency to pass something like this, that the Internet gaming was catching on, that California was going to be behind the curve; Nevada and some other states were poised to move forward. Has that occurred? And can you, again, paint a picture of the urgency in passing this type of legislation sooner than later?

MR. SHARP: You know, the urgency really stems from—and it did at that time and it does today as well from—the efforts on the federal level. That would include both Barney Frank's bill and also Senator Menendez's Internet poker bill as well.

With any legislation, it's always, you know, the seas are always changing, and it's difficult to tell how quickly it might move and what actions might take place to bring it to fruition. It's clear under those bills that California would be left out and you would receive, if you decided not to opt out, that you would receive very little from the Frank or Menendez legislation.

So in order to, as the chairman has suggested earlier to, capture as many dollars as possible and, frankly, to put in place regulation which to date simply

does not exist in terms of keeping underage folks off and helping problem gamblers and what have you, the thought was that we needed to move quickly in order to ensure that that legislation in Washington was not passed. Then we had a very short window to do something to opt out which might or might not happen; and then if it didn't happen, leave us in a very, a very poor position as Californians.

SENATOR WRIGHT: As we begin to look at again, this, as an issue, from my own vantage point, I would think again of this as an asset that the state has. And that's not to say that I would discount what you have and I would look at the tribal participation as being actually comparable to yours because, once you leave the reservation, they become not sovereigns any more but they're Californians just like you. Our mission would become, in short, to take this asset that we have and try to establish a value for it as best we can—how many people do we think play; what's the best?

I mean, we've heard several schemes today of how to best capture the revenue from an unlimited number of sites to a few sites. There's a monopoly site; there's the licensing site; there's the finite number. I mean, but our mission would be to figure out the best way to capture that value. Clearly, Mr. Chu and Mr. Sharp, from the side of poker, there's no one in the state that has more experience in the business of poker than you have.

On the other hand, Internet poker is kind of a hybrid from what you do. While the skills of the game are, in theory, the same, the actual computer modeling that occurs with it actually changes that dynamic somewhat. So even you would have to go and get someone who's skilled in that aspect of the business if you are running it because it does as well exceed—there's a difference between playing at the Hollywood Park Casino and playing Internet in terms of how you regulated it, how you control it, and all the other things.

Saying that, what would you suggest that separating out—how would you suggest we value this asset?

MR. CHU: I think, Chairman, you best described today, look at this as an asset, which is very, very true and, actually, this unfound asset. This is the group of people that this is unlike that, that the state would want to sell the Lottery. Okay. The Lottery is _____. The Lottery is actually—you're selling one of the net

worth to exchange for cash. This is something that they're already spending. There's 16 million people that spend money every day, and yet nothing stays in California. The state gets nothing. So this is an asset that's already been generated revenues for other people that, if the state regulates it, the state will be benefited by actually gaming tax or whatever....

SENATOR WRIGHT: Hold it a second—16 million is probably the highest number.

MR. CHU: Yes.

SENATOR WRIGHT: That's like half the state. That's probably high. I mean, I don't want to...

MR. CHU: It is high. But I was told they have records before that has 16 million names and phone numbers that actually play on Internet from California.

SENATOR WRIGHT: Okay. See, I'm from Chicago and, you know, we vote early and often but, I mean, that number seems a bit high...

MR. CHU: But they don't only play, you know...

SENATOR WRIGHT: But the argument that people have made is, since I can't tell you that it ain't 16 million no more than somebody else can tell me that it is because it is kind of, if this was algebra, it's an X right now. But a whole lot of people are playing, if we could agree there.

MR. CHU: Absolutely correct. A whole lot of people.

So what you had defined this as an asset is basically that we can actually get revenues from these people, just like on the Internet, they buy goods from outside of state and we don't get any taxes. So this basically is the same reasoning.

Now what you're seeing is, although we have brick-and-mortar experiences in managing people coming to play poker, how can we actually manage what they call the backroom technologies about all this? This is all software design by individual companies that license to all those Internet poker or casino operators for them to operate. The bigger operator basically develop their own software, but there are software companies that do nothing but to supply and provide, and provide, operators with this kind of software.

There's basically three pieces—number one is to operate. To operate, people get out to play to find which tables and all that; and then the money transaction; and security issue.

SENATOR WRIGHT: One of the concerns I would have—and I'm not even sure how to do what I'm describing—but just as you pointed out in the Internet, I mean, in California, when you buy something over the Internet, everybody here clearly files with the Franchise Tax Board that notice so that you pay the tax on that flat-screen TV that you bought from Amazon. I'm sure everybody in here does that as well as all the other things that you buy because it's one of the forms that you file.

But if we were to quantify the revenue that you receive from a player that goes into, say, Hollywood Park Casino, the concern that I would have is that we didn't alter the equation so that it suddenly became cheaper for the person to play online, in effect—let's say, again, the example that I have on utilities, which I've done a great deal more of, right now, if you buy satellite television, you don't pay local taxes to the city. If you buy Cable television and you get video from there, you do. So there is a tax advantage that is currently with the satellite broadcaster and you're watching people leave to avoid having to pay the local tax.

I'd be wary of creating another tax advantage or a regulatory advantage where a poker player who currently goes to the Hollywood Park Casino—from whom I get that 10 to 13 percent of the local; I get the income tax from you—you know, chances are, when he's there, he's going to buy a drink or a hotdog. I mean, all this money that I currently get from him, when he goes to that place, if he goes to the Internet, I forfeit all of that so that I can end up shifting a current player from a—and I'm just making up a number because I don't know. But let's say that you get \$4.20 an hour...

MR. CHU: I know what you mean, yes.

SENATOR WRIGHT: ...from a guy who comes to Hollywood Park, and I switch this guy to a place where I only get a buck and a quarter an hour. You know what I'm saying? I mean, I'm actually losing on a per-hour basis because there's less revenue that I get per player in this pot versus this pot.

MR. CHU: Playing poker is very different than playing slot machine or play Blackjack ??.

SENATOR WRIGHT: Right.

MR. CHU: There's intimidation factor in playing poker that a lot of people don't want to go to play to either casinos—they don't even want to play with their friends because the other guy's bullying him, look at him, and say he play, raise wrongly do this and that. They don't want to have that.

When you play this on the Internet, basically it's like you play slot machine. Why slot machine so popular? Slot machine so popular, it's because you play against a machine. If you make a mistake, nobody knows you make a mistake. A lot of people don't want to play on blackjack tables. Why? Because, if you're sitting at the last seat and you make a wrong move and the bank gets up to 21, you're in trouble. Everybody just stare at you and say, Why do you do that?

So that's why—there's a group of Internet players that will never get out to play. They will not. So you're talking about something that would be very small percentage of players that come to play poker. That's why—I did an experiment in my casino. I built a little, an electronic table. I find out my regular poker players just want to try to see what it looks like. Now you don't have to touch the cards. You go look at the cards like this way. I don't get any other people. From playing at home, people that come out to play in my casino. You know why? If they want to dress up, get in the car to drive to casino, number one, there are different places to pick, to play, and number two, they like to be social. Playing poker is a social game. You have to be playing with—it's a round game. The highest hand gets the pot so this is a round game. So each one play, look at each other. Why they wear dark glasses? They don't want to see because a lot of people, once they get two very good cards, they have a habit of touching their glass or touching this, touch their face, do something. The regular people that play with you all the time, they know whether you have a good hand or you have a bad hand already. That's why they wear dark glasses. You don't see their emotions.

So playing poker is very different than playing on something on the other games. The other game is strictly more of a gambling. But playing poker is a social game.

MR. SHARP: Mr. Chair, your question is a good one, though, that we would not certainly want to cannibalize the brick-and-mortar operations in favor of the Internet. But I think we're in agreement with previous panelists that you've heard from, and that is, that these really are—and I think, as Mr. Chu has articulated--these really are distinct groups. I think you would have to be sensitive to that, and the value of your asset would really be focused on drawing from the offshore, illegal sites. That's really where you want to draw from. You may have some new plays. We've heard from previous panelists, but you're really trying to draw from those offshore panelists. And we think, between the card rooms in California, the tribes—you have 90 card rooms; you have roughly 60 compacted tribes or gaming tribes. All those tribes would participate, however, that you really have a brand name there as well and that we provide that. We provide the marketing. We understand, as Mr. Chu's articulated as well, the psyche of the poker player—and while it may be on the Internet, the game is the same. You're still using strategies; you still have the vet/bet ?? mind of a poker player. And with our brand and the recognition, I think, by the people of the state of California that you have entrusted to us, poker, that we are licensed, that we are already vetted as being legitimate, same with the tribal casinos, that that goes a long way to moving those players. That is the best model for moving those players from these offshore sites to a state-sanctioned, recognized, licensed site that has people who have proven themselves.

SENATOR WRIGHT: Senator Negrete-McLeod.

SENATOR GLORIA NEGRETE McLEOD: If these people are already playing on off sites, why do you think there will be more people if it's legal? People like to do illegal stuff. So why do you think that you're going to get more people? I mean, I don't care if it's legal or illegal. I'm not going to play. If you make it legal, it doesn't interest me one iota.

MR. CHU: There are two issues where I think that the revenue will increase. Now if you look at, if you look at California gaming, tribal gaming probably is up to maybe \$8 billion. Okay. Now if you look at Internet poker, it's maybe \$300, \$350 million. Why? It's because all those poker players, because if it's legitimate—also, they have no way to trace them because they don't know

where the website is—they're mostly in Costa Rica, Venezuela, Gibraltar. So you know what? They play very small. They don't want to play big money because, if they win a pot of \$2,000, sometimes they tell them it's going to take you six weeks to get your money, and sometimes you never get your money so they have to fight. And since this is not legal, they can't call the police. They have no place to complain, no place that a consumer's regulation board that they can go to. So absolutely no way. So why? Okay. It's a little fun. I'm home. I wear my pajamas. I'm watching the football game. I play—actually, they can play two or three sites at the same time. So they just play a little bit small money. So most of the players on Internet poker, on those illegal sites, are all small players. Once you get into legitimate, okay. You have big names, like Agua Caliente, Commerce Club, Hollywood Park. I mean, they know where it is at. Okay. They win \$5,000. If they don't pay up right away, they call the DOJ; they call the commission; they call the local police. They know, they know where to go to get things settled because it's regulated; it's legal; it's under jurisdiction. So this is a big difference. So the difference to answer your question is really—I think this number is pre-legal website betting revenues—very, very small.

You can see, I think in Sweden, when they first took over—when they first legalized it, it's 30 percent. In two months, it went up to 88 percent.

SENATOR NEGRETE McLEOD: Eighty-eight percent of the entire population?

MR. CHU: No, no. Thirty-three percent is—let's say they have illegal gaming, X dollars. When they first legalized it, the legal websites only get 33 percent, only get one-third. As in two months, they turn over and they play on the legal sites.

SENATOR NEGRETE McLEOD: Okay. But it wasn't 80 percent of the entire population?

MR. CHU: No, no, no.

SENATOR NEGRETE McLEOD: Okay, okay.

MR. CHU: On the entire legal...

SENATOR NEGRETE McLEOD: When you said 16 million people are playing this illegal...

MR. CHU: It's accumulative...

SENATOR NEGRETE McLEOD: Yeah. So 16 million of the entire nation? Because I know you weren't talking about California.

MR. CHU: Entire nation is about 65 million people playing poker.

SENATOR WRIGHT: They count different? (Laughter)

SENATOR NEGRETE McLEOD: Because I know a lot of people. I have a lot of kids. I know a lot of people. So, I mean, I don't know anybody that plays poker on the thing.

SENATOR WRIGHT: Actually, you do. They just don't tell you. (Laughter)

SENATOR NEGRETE McLEOD: No. I would know, Mr. Wright.

MR. CHU: It's called kitchen-table poker.

MR. SHARP: And, Senator, I'm a perfect example of someone who would play—I don't play Internet poker now on offshore sites because I happen to agree with the director of the Bureau of Gambling Control, with Mr. Appelsmith, that it may very well be illegal to play, and I certainly don't want to jeopardize my law license or face prosecution from doing so.

However, I do play poker. And if there was a legal site in California and I knew that I would not be prosecuted, I would play poker on that site.

SENATOR WRIGHT: Let me say as well, though, not just as the Indian tribes or not monolithically in support or opposed, all the card clubs or likewise not monolithically in support or oppose, there are a couple of clubs who've contacted the committee to say that they're opposed to Internet poker. I mean, just in full disclosure, there's not kind of like a unanimous view from the card clubs or from the Indian tribes as to what makes, as to what makes good sense.

I think their concern was that they would end up seeing players that used to come into the casino switch, and they don't subscribe to Mr. Chu's argument that there's a social aspect to what they do. And, again, I don't know how to play at all, so I'm really not one to gauge. But the argument from, again, a couple of the clubs was that they would see people shift who used to come into the casino and that, you know, that would become a concern of theirs. I think...

SENATOR NEGRETE McLEOD: But wouldn't they be still getting revenue if they were playing on the computer but from the site?

SENATOR WRIGHT: Well, see, it's not clear because, if you crunch the revenue in a different fashion, the answer is kind of, sort of, maybe. I mean, see, it's not clear.

Let's say that a player plays on the website, depending upon how the website is structured, and let's say that that player lived in Inglewood and he was formally a player who played at Hollywood Park Casino but now he's playing on a different site. The revenue to Hollywood Park Casino might be a fraction of what he would have gotten because now there's a different way that the profit is split. So Hollywood Park may not end up getting the same amount of revenue from that player. The state might actually end up getting more revenue, depending upon how we structure the deal. But Hollywood Park or Artichoke Joe's or 101 ____, they could end up with less money if the player didn't come into the brick-and-mortar facility.

SENATOR NEGRETE McLEOD: However, then, it would beg the question, that if each club then had their own site, whether they came in to there or whether they played on the Internet site...

SENATOR WRIGHT: And you're right. We haven't—we're a long way from actually defining the scheme. So to your point, it could be that. It could be that, say Artichoke Joe's had their own site, then they would get the money from the people who played on their site, and that may be how the scheme—it could or it could not.

SENATOR NEGRETE McLEOD: Well, if I shop at Macy's, whether I go to the store or whether I buy online, Macy's is still getting the revenue.

SENATOR WRIGHT: Right, right.

MR. CHU: I think there's a difference. Yes, if you shop at Macy's, you have to pick a location. If you shop on Amazon.com, there is no location.

SENATOR NEGRETE McLEOD: No, no, no, no. What I said is, if you shop at Macy's or you shop online at Macy's...

MR. CHU: Oh, still get the revenue.

SENATOR NEGRETE McLEOD: ...so you could do Macy's, whether you do this site or this site, you're still shopping.

MR. CHU: You're absolutely correct. But now, what's happening now is, we have players, probably play onsite and also play on Internet, but we don't get anything from the things that they play on the Internet.

SENATOR WRIGHT: Right. And to your point, Mr. ____, you're right. If it wasn't a direct tie between the Internet site and Hollywood Park, then he'd still lose because they actually were playing at a different venue altogether so that could happen, or our scheme might be one where we had a revenue-sharing kind of agreement where all the card clubs and some pool of people got some portion of the cash, but that would still mean that he now would be sharing revenue that formally came to his place. But the other way to look at that is, if he didn't get any of it, he'd lose all of it. So is something better than nothing? Does he take a—I mean, those are all dynamics.

I think another advantage that you haven't mentioned but it was alluded to earlier, is that a state site could potentially offer something. Now this might be illegal; and fortunately, I'm not a lawyer, and there'll be lawyers who have looked at this before, but you might offer something like two nights at the Morongo Casino for some element of which you play. So there could be a spa night and something else as a feature of playing that probably again would not be offered by the offshore site because they're not here. So that potentially could be something that would be advantageous to, say, someone playing in California.

So let's say, that the people in Shingle Springs offered you one or that people at Morongo or at Borona, they have brick-and-mortar facilities that they could potentially tie in and extend the experience. But again, that assumes that they're also a part of the thing. Most of the casinos have restaurants that they could say, you know, if you win, you play so long, you get dinner at this place or—I mean, there's a different marketing aspect that you could have if we had a California site that may make it work. But I just wanted to make sure we all understood that not all the card clubs agree; not all of the Indian tribes agree. So there is kind of sort of a division among a lot of folks, and later we're going to hear from people who think we should get rid of all this gambling altogether, and they too have a valid point of view at the table.

Are there any other questions for the poker-club panel?

UNIDENTIFIED SPEAKER: _____? (Laughter)

SENATOR WRIGHT: But I've got this line written down. I'm trying to...

MR. CHU: Thank you.

SENATOR WRIGHT: Thank you so much.

MR. SHARP: Thank you very much.

SENATOR WRIGHT: We're going to call the next panel. We're just going to keep—these are the Internet service providers—and is Mr. Andrewes still here?

Mr. Andrewes (sp?), why don't we—I understand you're trying to catch a flight.

MR. ED ANDREWES: I _____, yeah.

SENATOR WRIGHT: Okay. You know what? Why don't you crank up first. And if you're leaving at 4 o'clock, though, you're going to be quick 'cause...

MR. ANDREWES: Yeah. Well, my flight's at 5:15 actually.

SENATOR WRIGHT: Oh, okay. All right. Okay. Mr. Andrewes, why don't you go ahead and get started. Mr. Andrewes is the managing director of Online Gaming, Ladbrokes. Okay. Go ahead, sir.

MR. ROBERTO SAVIO: My name is Roberto Savio.

SENATOR WRIGHT: No. I'm going to...

MR. ANDREWES: I think I'm going to start.

SENATOR WRIGHT: I'm going to let him—he's trying to catch a plane.

MR. ANDREWES: Well, thank you.

SENATOR WRIGHT: Normally, I would have done that, but I'm just deferring to him to try to catch an airplane.

Okay. Go ahead.

MR. ANDREWES: Well, thank you very much, Mr. Chairman, for giving us the opportunity to be here. I think it's been a very interesting debate, and I think a lot of the key points certainly, as an operator, I think, have already been covered, so I thought I'd focus on a few specific areas.

Just for those of you who don't, just a quick introduction to Ladbrokes. We're actually the oldest betting company in the world, sports-betting company in the world, founded in 1886. We're a 5250 ?? company, market cap of over \$2.5 billion U.S. We've got over 3,000 retail outlets around the world. We operate—we

have seven bases internationally and operate under five different licenses. And we have a sizeable online business of which I'm the managing director. I thought of all the arguments we've heard today. I think probably the one key-specific thing I'd like to take out is, Is this business about why would players come off the illegal sites and come and play with a intrastate site? And there's been a lot of debate. You know, they've got to be incentivized; they got to make it easy.

I think the key thing is actually, players want to play on regulated sites. They want to play where they can find the trust and have the trust, and I think it's very important that that is shown within these regulations. We actually operate, as most of the operators on the panel, around three key principles laid out in the 2005 Gambling Act in the U.K., and that's to keep online gaming crime free, to conduct online gaming in a fair and honest fashion, and to protect the young and the vulnerable.

And we've heard a lot the arguments already this afternoon about how we do this, how technology helps us do this. In fact, in many ways, things like protection and keeping crime free easier to do online because, as you've heard, you've got the data and systems in place. And just in terms of the crime aspect, every single one of our customers by law are under money-laundering legislation and law in general, we have to know each customer. So each customer, when they come, is verified and that happens automatically against a database. And if they fail on that database, then we'll contact them individually and verify who they are. So it obviously helps with crime and also helps in making sure that everybody who comes to play with us is overage.

The Internet allows us to monitor play far more closely than you would in an offline outlet. We have real-time systems in terms of tickers and monitors where we can see people as they register; we can see the game play as it happens; we can see every time people deposit; and our team of security people will have the alerts and be watching to make sure this happens.

In terms of fair and honest, again, we have the systems in place. We've touched upon it in earlier discussions about the collusion element and how, particularly within poker, that needs to be, that needs to be curbed. And you know, we shouldn't allow people to collude and effectively cheat against others.

We have the geo-location software so that we know where players are and we know that they're working in syndicates. And again, protection of the young—everybody's—protection of the young and the vulnerable, everybody verified for age when they come on.

In terms of people who may be problem gamblers, far easier to regulate online how much a player is spending online rather than is offline. So we set deposit limits. When every customer registers, they say how much money they want to deposit with us over a variety of time periods, be it 24 hours a week or a month, they can say they only want to deposit certain amounts.

We have an exclusion policy. If somebody rings up an exclusion and says, you know, we don't want to bet any more, they get excluded. It then takes them six months. They're excluded for at least six months. And if they come back and approach us and say, I actually want to start playing again, we don't let them play instantaneously. We talk to them. And if we feel they're ready to go back and play, then we give them 24 hours cooling period. They can't come straight on and play.

And again, as we've heard, monitor behavior. So if we think somebody is having a problem controlling their gambling, then our customer services staff are trained to look out for it and trained how to deal with it and we'll refer them onto one of the agencies that can help with it, mostly usually GamCare ??.

So I think, really, of all the things we've heard from an operator's point of view, that's the bit I wanted to stress, as well as the revenues that come in. You want to set up a system that's well regulated because, as everybody knows, those players are going to go on playing, so why not have them playing where they know they can be playing with a well-regulated, fair and honest, and an operator that's going to look after them?

SENATOR WRIGHT: Okay.

MR. ANDREWES: Thank you, Mr. Chairman.

SENATOR WRIGHT: Stay as long as you can.

We're going to move now to the Ferrari pen guy—I'm sorry—Robert Savio.

MR. SAVIO: Roberto Savio.

SENATOR WRIGHT: Roberto.

MR. SAVIO: Roberto.

Mr. Chairman, I'm happy to say that we figured out who has traveled the longest distance and it's actually not me. It's Jonas Söderlund, which beat me with 30 miles. So whatever prize you figure out, we have to take that with him later on.

I think I would like to start, just a bit retrospective. Meanwhile, we are debating this here today if and when it should come. Internet gaming, and especially poker, has been, online poker, has been on the market for almost 15 years. So meanwhile we're debating this, somebody obviously have taken great advantage to build a technology platform and operational malls ???. And nowadays, those systems are very much _____. Again, it's a highly lucrative business which you as a state, as well as the common operators could both gain from. So in my perspective, I see more of a win-win relation than something else.

Some of those things again have been covered several times today. I was here actually in December in Sacramento 2008. And as you said, rightfully, before, the understanding and awareness about online poker has raised significantly here which is a very positive thing, I have to say.

But again, just to stress the factors, if you want to do a successful online poker operation, you have to be sure that you can do integrity, transparency, and certification, data security and integrity platforms, availability, of course, when it's people playing to people, customer service, and, again, marketing. And as a lot of my colleagues already said today, to be playing in a safe and regulated environment is a very, very important and powerful thing, and I will come back to the Swedish model a bit later.

When Svenska Spel launched the poker in Sweden for about two-and-a-half years ago, during the opening day, myself, including approximately 20 percent of the 300,000 poker players in Sweden, of the 9 ?? millions, 20 percent in the first two hours downloaded the poker software. I'm not saying that everybody deposit money and played, but that was fact. And all those players had obviously before been playing on unregulated and untaxed offshore sites. So I think, even for Svenska Spel, everybody on the market, including myself, was surprised about the impact of a safe and regulated market which is of extreme importance. I think I

cannot stress that enough. And for the same reasons, as we have been discussing today, France, Italy, Norway, Holland, I mean, all is looking in the same way and they all see the benefits from this, which takes me to the PowerPoint slide I prepared today coming in here to see that there were no machine to show the pictures. So I prepared pictures actually called Operation Win Back because that is actually what you have to do. And correctly, as you've already said today, this has been going on for such a long time. It's not a question about nothing or a bit. It's out there and you can grab it if you want to.

And the problem here for you is not how the existing land-based gaming providers will lose money if/when this comes through. It's not however California would lose income taxes when/if this comes through. The problem is that somebody right now is taking your money, and I'm glad to see that that is actually coming through and you are very well much aware about that, so I will not tire you by discussing that any more.

But in my opinion, your first target here, or your colleagues, which will be the land-based operators, what they should do, of course, is to after the already playing people on offshore sites, and they are creating those giant revenue streams. Meanwhile, we have been debating here today. Possibly the offshore company has earned about—I mean, I hate to say numbers because you will always be questioned, but let's put a number—about a million bucks, just today. And the interesting part, the only thing this place can rely on, is the goodwill from the operators out there when it comes to cash out and that they actually have payment solutions working for them, which is not an actual thing today.

So taking that perspective into if it was a legalized business where the state were standing behind people actually getting the money, I think it's pretty obvious where we're going. And I think the important thing here is actually—I dare say that, no doubt, the opening day here, if/when it comes, will have about the same impact. Everybody will know it. Everybody will be curious. A lot of people will actually download the new poker client. So that is the not the issue. The issue is, How do you keep them motivated to stay and deposit money and play on the state-regulated sites? I think that is the big question, which takes us more to actually,

not an acquisition model on the customers, which a lot of people tend to see. I would call it more of an attention model.

And how that could be, of course, that is, I mean, and faces ?? on the safe and regulated environment? The marketing money spent on the existing casino's poker clubs, et cetera, and the good benefit that the clubs here and the casinos have is that they meet a lot of their customers face to face, which means they can actually use that as a good marketing window to promote and win those customers that are today playing elsewhere.

And, of course, the marketing from the state telling the population that this is regulated and now safe to play is, of course, big—maybe we shouldn't call it marketing but informing the population about that. But again, I mean, it's going to be hard work. It's not going to be a walk in the park. Everybody has to fight for the money coming in. We know that those operators out there today is gaining a lot of money. They have done those for several years, and they are extremely professional. But still it's, for me, to end this presentation, I think it's very clear that it's a win-win situation.

It's a win for the company who provides the technology; it's a win from the land-based clubs and casinos; it's a definitely a win for the state; everybody will earn money from it. But my last sentence here will be that, if you cannot work this out, ending up in debating things that is not really what we're talking about, then those other sites, offshore sites, will continue taking the money which, in my perspective, rightfully belongs to you.

Thank you.

SENATOR WRIGHT: Thank you, and I hope you have time to stay because...

MR. SAVIO: Sure.

SENATOR WRIGHT: ...we probably have questions for this panel.

Gerrard Cunningham, Betfair.

MR. GERRARD CUNNINGHAM: Thank you. Gerrard Cunningham, president of TVG and BetFair USA.

Now that we've established who's come the furthest, can I put my hat in the ring for who's come the least distance? I came up from San Francisco today, and

this accent of mine does give me away as being British. But actually having living all over Europe, all over Asia, I chose California as my home 15 years ago. I love this state very much, and I would like to do what I can with our company to help us reclaim the lost tax revenues and be able to protect our residents from the offshore illegals for not providing protection they need.

As I mentioned, I run Betfair USA. The parent company is Betfair. Betfair Limited is the largest legal online betting community in the world. We've got the highest standards of integrity in the online world. When I say *legal*, our company, Betfair, never took bets from the USA even before UIGEA. Our standards of integrity were so high, we said that this a grey market and that we would stay away from it and we were proven right. And when I say *largest*, we now are about to overtake the New York Stock Exchange in terms of the number of bets that we take every single day and so the number of transactions, and that's across poker, casino, horse wagering, and other sports wagering.

As one of the largest online operators with more than ten years' experience in the online wagering industry, we built the largest integrity unit in the industry. The integrity unit looks after security, fraud, cheating, collusion, anti-money laundering, underage protection, problem gambling, as well as regulator reporting. These are all very, very serious issues that are very complex and need to be managed separately than in the physical world.

The integrity team uses a series of analytical tools as well as human interactions to identify potential problems. We work very, very closely with regulators in every jurisdiction that we work; we've brought those same standards to the USA; and we have cooperated in a large number of investigations around the world. You've probably seen some of the way we've shared the transaction data with the state regulators. We've put it together with telephone data to be able to track down how people have colluded and cheated.

It's worth pointing out that every year in the UK, there's a mystery-shopping expedition done by the regulators trying to get underage wagers onto the various websites in the UK, and we're the only company that every single year defeats those regulators on a consistent basis. And it's worth just adding this, for Betfair, as a highly regulated business, we have no interest in making any money from any

of these potential problem areas. It is of no benefit to us to have problem gamblers, underage gamblers, or people cheating. What we want is a completely safe environment where people have got complete trust in the online experience.

Turning to the U.S., we run here a company called TVG. TVG.com is the largest legal operator of online wagering in the USA. Our business is taking bets on horse races. We place those bets into the tote system at each track where we have contracts. For eight years, we've operated TVG.com across the USA and follow very tight regulatory policy. We now take wages in 17 states where we believe it is completely legal. We have 200 jobs across the USA, including 150 jobs here in the state of California.

The identity confirmation, age verification, geo-location, technology you've heard being discussed here today is already in place at TVG. We use that every single day when we register new players and when we, when we take their bets every day. And we are also working very closely with the regulators here in the U.S. We've now placed bet monitoring systems—we've offered it to all regulators across the U.S. We now have it in place in the state of Oregon, in the state of Virginia, where they are able to see the transactions going through our system on a ___ basis so they can identify any problems.

As I've already mentioned, California is losing tax revenue to illegal offshore operators. We commissioned a study by GBGC, one of the leading consultants in the world in this area. I think that is in your package. And they helped us size the market and estimate the lost tax revenue. To clarify some of the numbers earlier, the U.S. alone, we believe in 2010, there will be about \$1.5 billion that leave the USA to the illegal operators from about 3 million players. And here in the state of California, it is about \$450 million a year, and there's about \$800,000—800,000 players—here in the state of California actively playing on an annual basis.

And if regulation takes place, the estimation from GBGC is that we could expect the market to grow dramatically. You've heard some of the reasons why, in terms of customers feeling safer, more secure. We would expect California to be a \$900 revenue million business, of which, of course, you can then set tax. Achieving this kind of growth, ensuring the state maximizes its tax revenue from

online poker, requires that the operators in the market can compete against the illegals and do so using innovation.

This is an incredibly fast-moving industry. We've heard how the industry is only 12 or 14 years old. It's already gone through several waves of technology innovation where leaders around the world have been crushed by the next wave of technology leaders. If we get into a stagnant situation where innovation cannot occur, then the state of California will be left behind. And if we want to compete against these and capture this lost tax revenue, we believe it requires an open, competitive market that encourage that innovation in technology, in marketing, in customer service.

The state needs very clearly a strict licensing regime that limits operators to those with high standing, the financial wherewithal, in addition, the capability to operate an online business, and the capability should be audited before switching on the online business, and audited on an ongoing basis by the state. We've seen that as the best practices around the world.

In closing, the best practices around the world have shown to us that in this fast-moving market for California to maximize tax revenue and to compete with the illegals, California needs an open competitive market. As we go forward, please consider myself and my company completely at your service. We'll help you find any information you need.

SENATOR WRIGHT: Thank you.

Mr. Barry from Sportsbet.

MR. CORMAC BARRY: How ya doin'? My name is Cormac Barry. I work for Sportsbet.

SENATOR WRIGHT: A lot of you guys from Britain do this.

MR. BARRY: Sorry? (Laughter)

SENATOR WRIGHT: Actually, you're Australian?

MR. BARRY: I actually win the prize for coming the furthest distance because I came from Melbourne, Australia, to come here today.

SENATOR WRIGHT: Give that man an aerator ???. (Laughter)

MR. BARRY: Yes, I am Irish and Paddy Power is an Irish company that's been in operation for the last 21 years. It's similar to Ladbrokes, a multi-channel

gambling operator, that operates betting, sports betting, poker and—thank you very much—and a casino, amongst other things. We are listed on the Dublin and London Stock Exchanges and have a market capital of approximately \$1.5 billion and have a turnover of over \$3 billion.

We have been in the online poker business since 2005. And as a public company that is prudently managed, we only operate in licensed and regulated markets, so we hold licenses in countries like Ireland, Australia, the UK, the Isle of Man, Alderney, Malta. And, you know, what slightly hasn't been said is that the reason why people ended up in these offshore locations is because the mainstream locations didn't allow them to ___ and set up their business in those locations. So the desire is always, particularly for a public company that wants consistent and sustainable revenues is, to invest in the sustained and regulated market, and then you can justify the considerable capital investment to get the return.

So there is always a desire on the part of the mainstream regulated operators to invest in, you know, good jurisdictions that are well regulated. And Paddy Power was also recently selected by the PMU, which is the French betting state monopoly, to assist in sports betting, and we are also ___ with Betfair, one of the very few online operators to have never taken any play from U.S. customers.

We really appreciate the opportunity today to give you an insight into the motivations of the private operators who exist in what is now a global industry. And we also would like to share our views on the attractiveness of the California market and the regulatory system that you should adopt.

Much of this has been covered, but I'd just like to reiterate, from the point of the private operators, that we believe the optimal model is an open, regulated system with unlimited licenses that allows and stimulates innovation, as my colleague here from Betfair referenced. It will also give the consumer a better product; it will maximize employment; and it will maximize tax stake for the state of California.

You alluded earlier that it might take a considerable amount of time, two to three years, to get a system up and running. I would argue, that, you know, subsequent to legislation being past and your getting through the various legal issues that may ___, that you could have a system up and running in six to nine

months, and there is a queue of private online operators, along with the Nevada operators, who would be very keen to enter this market. And no one has actually today put a number on how much revenue you guys could actually raise. Based on the same research that Gerrard was referring to from GBGC and some other research, I believe in year one you could raise \$30 to \$50 million, and this would rise to sort of \$150 to \$200 million within three years.

And the model I would suggest that you should take on board is that you have a significant license fee, and I believe you could charge a significantly larger license fee than the Italian government has, which was referred to earlier, of €350,000. The desire of foreign companies to get access to the U.S. market and to be an early adopter within the U.S. market, you could easily be charging single-digit millions as license fees, and I would also suggest you could charge a higher surcharge on the rake than has been suggested in France, single digit, to remain competitive versus the offshore competitors but, you know, in the range of 5, maybe 7 percent.

So I believe this is a much larger opportunity than has been alluded to earlier by the various contributors. I also would dispute the contention that the introduction of online poker will have a negative impact on the land-based gaming operations, whether the card clubs or the casinos. And the growth in the Indian casinos was at its greatest from 2004 to 2006, which is when online poker exploded within the U.S. And a similar phenomenon occurred within the card clubs. And as people became more exposed to online gaming and online poker, it drove them to the land base and a rising tide lifted all boats. Once again, if people have certainty of entry and they know that they can get a license for a significant period of time, whether that be five or ten years' time, they will have the motivation to invest significant capital in marketing which will stimulate demand and also relieve the significant pent-up demand which has been referred to repeatedly.

I had dinner with a poker player last night and the lady repeatedly tried to explain to me how difficult it is to get money in and out of an offshore site and the very, very low probability of you getting paid. A significant number of Americans have given up playing online poker because it is too difficult to get money in and out, and a significant number of players have stopped playing because they got

letters from their banks saying, if you use your credit card, you know, we're going to come after you and we're going to seize those funds. So I think there is a very significant pent-up demand which will be positive for the online poker industry and would also be positive for the gaming sector in California as a whole.

One other issue that hasn't been alluded to today is the potential for—we've only talked about intrastate gambling, and that is, you know, the subject matter of the committee. But there is also, I understand from my legal counsel, the possibility of mutual recognition of interstate jurisdiction, so there could be a scenario where, if Florida recognizes poker, their ___ regime could be mutually recognized by California which increases the pool. That also increases your motivation for California to be an early adopter in this space and to become the center of excellence within America.

California has a proven reputation as a market leader in entertainment and online services by, you know, the movie industry and Google and eBay and those types of companies, and there is a unique opportunity here for California to move first, become the center of excellence for online poker, not just within America but worldwide. California has the market size; it has the demand; it has the human capital; and is almost uniquely positioned to take this opportunity now. And at some point, some other state within America is going to grasp this opportunity, and that will be the state where all these foreign operators will set up and locate.

In terms of valuing the asset—I mean, I've discussed what I think the potential tax revenue—typically, a company like Paddy Power would go in and employ 100 to 200 people quite quickly. Betfair referred to a similar number to run an online horseracing site. It's a similar number of people to run an online poker business. And if you had ten to 20 to 30 entrants, obviously, you know, you're getting into thousands of jobs which is all the significant lock onto benefits. You also have all the significant lock onto to benefits of marketing spent and technical jobs and design and the spin-off on all the services they will use.

So in summary, once again, just to reiterate, it needs to be an open market; it needs to be highly regulated; we need to protect the players; we need a tax system that is fair and doesn't overly disadvantage the regulated operators versus the offshore operators. But I believe there's a unique opportunity here for

California to take the lead in this industry, and that will position you for the future to be a dominant player in this place.

SENATOR WRIGHT: Okay. Thank you much. If you'll hold on, I'm going to move to Mr. Goldberg.

MR. DAVID GOLDBERG: Thank you.

While Cormac does have to go back to Melbourne and I'm only going to Los Angeles, I do have to go up the 405 to get home, so it's possible he might get home before I do. (Laughter)

Good afternoon, Mr. Chairman, Members of the Committee, my name is David Goldberg. I'm the president and CEO of Youbet.com, a California-based company, and one of the largest legal online wagering sites in the U.S. Our company operates under the Interstate Horse Racing Act of 1978, and we only accept wagers on horseracing, pari-mutuel horseracing. I should note that Youbet and Churchill Downs, owner of the Kentucky Derby, recently announced a transaction where Churchill will acquire Youbet but that deal is not closed, and I am here speaking solely on behalf of Youbet.com.

For the California legislature, the approach to Internet gambling in general and Internet poker specifically needs to be considered in the larger context of the ever-expanding opportunities brought about by the Internet and the expansion of recreational activities for adults. With the exception of pari-mutuel horseracing, Internet gambling is completely underground, as far as the U.S. is concerned, untaxed and unregulated. Young people and problem gamblers are particularly ill-served by the current system. They have unfettered access to a product that is outside the jurisdiction of the United States and California authorities. And as a result, the many programs and compliance measures that we use to keep them from gambling are not utilized.

The fact is, gambling is a widespread activity. And when properly regulated, it's generally accepted. And why not? It's really a matter of personal freedom and common sense.

One only need to look at lottery sales, bingo halls, charitable gaming festivals, pari-mutuel, and other casino gambling facilities throughout the country to see that legal forms of bricks-and-mortar wagering are established, accepted,

and regulated in our country. So why should most forms of online gambling be illegal?

The overwhelming majority of Californians who gamble online are otherwise law-abiding citizens who want to wager on a system that has integrity and security. In this Internet age, it's very difficult to slow down Internet gambling, much less stop it. The only way to put controls on Internet gambling is to legalize it, regulate it, and enforce those regulations against the violators.

I do understand that in the legislative process, what should be done and what can be done are not often in alignment. I'm here to tell you that the technology exists and is in use today to ensure that online Internet gambling, including poker, can be effectively regulated and taxed. I can say this with authority because at Youbet, we are first and foremost technology people. We understand how to run an ecommerce business—what works and what does not.

Other members of our Youbet senior management team and myself have been executives at leading-edge technology companies, such as Orbitz, Ticketmaster, Careerbuilder.com, and network Solutions, and we understand how technology can be used to safeguard consumers. I understand the concerns about underage gambling. As a parent, I want to see online gambling legalized. So why would I say that? Because I want it managed properly.

Today's out-of-control Internet gambling situation was made possible by the revolution in technology, and it will take technology to fix it. Today at Youbet, we already use technology that would ensure effective regulation of a variety of forms of Internet gambling, including poker. Online pari-mutuel wagering on horseracing, which already exists as a legal and regulated activity, is a U.S.-based model of how to provide a responsible online wagering experience for adults, one that is clean, regulated, and scrupulous about both collecting and paying taxes.

Youbet.com uses the latest technology and vigorously maintains its own responsible wagering program. We developed it over the 13 years that we've been in business. It's designed to prevent underage gambling and provides tools to combat problem wagering. The technology enables us to conform to federal laws and the laws of those states in which we operate, California among them, including meeting all tax withholding and reporting requirements.

A second critical point to note here is that the Internet is as successful as it is because it is open. The power of the Internet reflects the power of the consumer. On the Internet, the consumer decides who wins and who loses, as it should be. Any regulations put in place by the legislature should reflect the democratic culture of the Internet. No single company or entity should be favored over another, providing that they have complied and are able to comply with the regulations. At Youbet, we're proud of our standing as a premier online pari-mutuel horserace wagering company. We did it the traditional way, through hard work and technological expertise.

As you know, the U.S. Congress is considering legislation addressing online gambling activities. The executive chairman of Youbet, Michael Brodsky, recently testified before Chairman Barney Frank and the U.S. House Financial Services Committee. Mr. Brodsky had a similar message to mine: Internet gambling should be legalized and regulated using technology available and in use today.

Now also at that hearing in Washington was Parry Aftab. She's the executive director of WiredSafety. That's the world's largest and oldest Internet safety organization. Ms. Aftab is also the author of the *The Parents' Guide to Protecting Your Children in Cyberspace*. She had this to say, and I'm quoting:

"Most people are aware of the moral arguments against gambling. A lot of people are aware of the regulatory and legal issues. Few of them understand that this really is a consumer protection problem."

Ms. Aftab went on to say:

"That the only way to protect consumers from online gambling risk is by legalizing it."

At the same hearing, Professor Malcolm Sparrow of Harvard's Kennedy School of Government, testified to the efficacy of technologies and procedures to ensure a robust regulatory structure. He submitted a report that I'm happy to make available to this committee.

While Ms. Aftab and Professor Sparrow were addressing the national scope of the issue, the fact is, this is an area where California can lead. For California, legalizing, regulating, enforcing, and taxing online poker means providing a safe alternative to the offshore black market that allows easy access for anyone with a

computer and an Internet connection. If structured and implemented correctly, it will provide a properly regulated environment where consumers will decide what works and what doesn't, knowing that they will have recourse, should an issue arise. And, yes, it means additional revenue for California that today is being funneled offshore.

I hope the committee considers all the important matters surrounding this issue and ultimately decides that a properly regulated, consumer friendly, and transparent Internet watering market, filled with choice, is preferable to the current underground environment. We have the technological tools to help you enforce the regulatory architecture and look forward to working with you in the months ahead.

Thanks for the opportunity to testify and with the rest of the panel. I look forward to answering any questions you might have.

SENATOR WRIGHT: Well, last on this panel, Mr. Painter. And for people in the audience, this is an addition. Scott Painter is the founder of United States Digital Gaming.

MR. SCOTT PAINTER: Mr. Chairman, Senators, thank you very much for holding the hearing today and also allowing me to speak at the last minute.

I'm a technology entrepreneur and I've built over 30 companies leveraging computer technology and the Internet, and I've raised about a billion dollars for those businesses.

I'm here today because I represent a high-profile group of investors that have taken serious interest in the explosive global growth that's occurring in the Internet gaming space. And California, unarguably, represents one of the largest markets in the world and the question before this panel is, if, when and how California will participate in this new growth industry.

Not only will you have to properly determine the size of the opportunity—and a lot of people have spoken to that today—but more importantly, you're going to need to identify the risks and concerns that must be addressed. As well, you'll need to determine the most effective approach to enabling this market while addressing those concerns.

So first things first—and I think you’ve heard it pretty articulately from this panel—I think that the technology, it’s safe to say, does exist. Today, there are clearly technologies that can provide very secure player registration and authentication; the administrative controls to prevent illegal or irresponsible gambling do exist; the game technology to allow for robust play is actually quite remarkable—the intellectual property in this space has exploded in the last couple of years—security controls to ensure gaming integrity against collusion or fraud or bots, as have been referenced today—they’re all in place; the banking and the payment technology to facilitate not only micropayment but immediate taxation also exists; and there are lots of other technologies that also become part of this overall ecosystem.

However, despite all of that, it’s worth noting that none of these systems are currently developed or currently deployed on an integrated basis here in the U.S. market for the individual niche solutions that will be required on a state-by-state basis. Clearly, California’s going to be a unique case in terms of how you navigate all of the issues that you’ve been discussing today. But the simple fact is, because the issue of legality exists, any investment becomes a speculative bet. So other jurisdictions, clearly France, the UK, Italy, Sweden, Canada, even horse betting here in the U.S.—and actually if the last gentleman had used the British accent, I was going to try one as well—they’re all operating similar platforms that could provide a shortcut for entering this market.

That said, the specific approach to constructing and deploying the appropriate infrastructure is the issue and the key to fully realizing the opportunity for the state. Clearly, California has numerous issues to navigate with respect to existing licensees and compacts, the geo-identification of players and where a session begins and ends, responsible gaming, player registration, game integrity, compliance with federal laws, the flow of funds—do the funds, you know, begin, originate in the state, and then end in the state?—taxation, and, of course, enforcement. That said, California can and should lead the nation with a model for the legalization of Internet poker that unleashes the power of an open market and open-market competition while establishing a framework that is secure, manageable, robust, scalable, and immediately taxable.

In the Internet and technology terms, the solution is to create a standardized technology, security, and banking platform that can be licensed to all of the licensed operators. These operators would then be able to personalize the technology, or white label it, so that the individual brands could market and grow their player base independently. This would allow for whether it's an Indian tribe, an existing casino operator, a new entrant into the market that qualifies for licensing, or any others that have the state's approval to do so. They would have the advantage of being immediately compliant but also independently brandable.

Individual games could be deployed and developed by independent operators through an open-architecture approach that would be game agnostic so long as the registration, security, banking, ad-service, ecommerce, and related components that ensure security, integrity, administration, related revenue, and taxability are used by licensed operators.

It's only through this type of approach, commonly referred to as a *walled garden*, that the state of California can effectively manage this process and efficiently unleash both the open-market opportunity and the related growth that technology investment and development will certainly follow. Legislation has absolutely been proven as a way to unleash new industries and wealth creation.

It's intuitive to understand that the legalization of online poker in California will certainly grow the size of the existing market, create new tax revenue, and prevent the exportation of gaming dollars to other jurisdictions. That said, that isn't the end of the argument for online poker. We believe that the bigger question is whether or not California wants to leverage its inherent advantage as the cradle of technology innovation and lead the nation and, in fact, lead the world in this opportunity.

The gaming industry is about to go through a boom, irrespective of when our state does join the race. That said, this is an opportunity for California to create jobs, to generate tax revenue, and to lead in the investment and innovation and the development of one of the most explosive opportunities in recent years. Thank you.

SENATOR WRIGHT: Thank you.

Any question for this panel? Now it's just me and you again. He snuck away. Okay. Any questions?

Now all of you operate gambling platforms; is that—I mean, in one sense or another—currently? So the ability to control for access by underaged participants, you've all had to navigate that all?

UNIDENTIFIED SPEAKER: Um-hmm.

UNIDENTIFIED SPEAKER: Correct.

UNIDENTIFIED SPEAKER: Yes.

SENATOR WRIGHT: So we can fairly comfortably say that that's something that's manageable?

UNIDENTIFIED SPEAKER: Correct.

UNIDENTIFIED SPEAKER: Yes.

UNIDENTIFIED SPEAKER: Correct.

UNIDENTIFIED SPEAKER: Yeah.

SENATOR WRIGHT: The location of the player is something—I mean, we would have to, notwithstanding if we had a reciprocal agreement with another state—we would also have to allow for being able to say that it was a California player so we'd have to be able to certify to the federal government that we weren't taking players from Pennsylvania or Nevada or Florida or something?

MR. CUNNINGHAM: Right. A California-based player who is actually in California at the time of starting a new game.

SENATOR WRIGHT: Would you look to try to in any way block the offshore player or just hope that the security of the game would motivate the player to move?

MR. CUNNINGHAM: We would love you to try and block the offshore players. I don't think that would be our role. We would also be probably be seeking that you bring the full force of law against those who are breaking the law and bringing games to players in the state in an unlicensed way, in the same way as in the state of Nevada. If someone opens an unlicensed casino, then the law would go after them.

SENATOR WRIGHT: I saw a piece of software a couple of weeks ago, that when you signed on into this software, I guess this software places something in

your computer that actually would have prevented you to going to the online site. The concern that I had with that, it would seem to me that that would restrict you from wanting to put that device on your computer because it would limit your access of what you could do with the computer. The concern would be that you don't want to make the California site something that provides its own reason for people not to want to play it. I mean, the other issue—I mean, even limiting—I mean, if I'm going to bet again, that people who are going to play this, that the big money really is going to be in the smaller dollar player, that you'd have a whole lot of people who would play in the \$200, \$300 range as opposed to the high rollers. I mean, the slot machines tend to do—the quarter and 50-cent slots do—a whole lot more business than probably—you know, it's been my experience at the casinos—than do the high-roller tables.

MR. BARRY: Yeah. I mean, I would believe it would be possible to inquire cooperation with the ISPs to geo-block. I mean, Paddy Power geo-blocks all U.S. play, and there's other jurisdictions. We would consciously not allow people to log in from—and that would also be ___ payments. And one of the earlier...

SENATOR WRIGHT: But you do it—but Paddy Power blocks the U.S. player from coming in.

MR. BARRY: Yeah.

SENATOR WRIGHT: But the U.S. site doesn't block the person from going to Paddy Power. You block it going this way as opposed to attempting to block it from going out. So I guess there would be a difference because clearly the offshore operator has no desire to block people from coming in because he knows full well that that's his business, is to attract people from outside.

MR. BARRY: Yeah. I mean, I think you'll struggle to block people going to illegal operators.

SENATOR WRIGHT: Okay.

MR. PAINTER: Mr. Chairman, I think one of the issues is, clearly, Mr. Chairman, people are going to still gamble illegally. The decision whether to gamble at a legal site versus whether to gamble at an illegal site is going to be based on the experience and whether or not it is, you know, from a either safety or game integrity point of view or from an ability to enforce any kind of action against

that site more appealing for them to stay in a legal environment. I think that obviously, the more you open the market to competition and enable all entrants who want to play by those set of rules, the more you're going to take the interest away from illegal opportunities where people would otherwise have to be sort of without that safety net.

SENATOR WRIGHT: So all of you—I'm sorry—Senator Negrete McLeod.

SENATOR NEGRETE McLEOD: What differentiates—actually, I feel like I'm in a foreign movie. (Laughter) I go to a lot of foreign movies. What differentiates between a legal and an illegal? Do you have little signs—legal, illegal?

MR. SAVIO: You would not have the illegal one. (Laughter)

SENATOR NEGRETE McLEOD: No. I mean, right now, all of the sites that you're saying are illegal. So what differentiates?

MR. CUNNINGHAM: Can I just say, I mean, one of the—if you look at the people on this panel, the people who are from overseas, are ones who have not broken the law here in the USA. What you are missing are the two biggest poker companies in the world. There are another ten or 15 who are taking bets throughout the world quite happily and are taking bets from the USA.

Now while there are arguments that say some of the laws in the USA are grey, the fact that they are not present here probably shows you that they feel at risk in some way. So you're quite right, Senator. There is no sign on the websites. What you have to do is dig down to a level of detail and look at the regulatory policy of these companies and whether they really do want to follow the laws of the states in which they operate.

MR. GOLDBERG: Well, and that's just it, is we all operate under licenses and regulations and choose to operate legally. There are plenty of others out there who choose to ignore those licenses and regulations and operate illegally. But it is incumbent now on the consumer to do their homework to make sure where they're placing their bets.

MR. PAINTER: Senator, I would also add to that, that this one of the key issues that this panel would have to really investigate. And the ability to actually register to gamble in the same way that you register for a driver's license is one very clear way to enforce all of the things that we've been talking about today, from

underage gambling, to problem gambling, to administrative controls. And doing that on some kind of a centralized platform, that all of the constituent operators can operate from, ensures that the flow of funds that the registration and tracking of play and the enforcement of all of that from a both technology and security point of view can all be administrated. That is one possible solution; and obviously, that's not something that's being voted on or is being yet proposed. But I think that that is really sort of the next step, is, Are there ways to approach this architecturally at a state level prior to making it legal that do make all of these things possible?

Today the environment is very much a Wild West where, what you have here today on this panel is predominantly, you know, compliant operators who are operating in a way that we would absolutely embrace, and I think that what we're not wanting to necessarily rely on is just that kind of upstanding behavior. I mean, we want to have a system that actually allows us to regulate it with much more predictability and enforceability.

MR. CUNNINGHAM: Excuse me. Could I just follow up on that?

SENATOR WRIGHT: Sure.

MR. CUNNINGHAM: I think it's very important that two of these companies actually do operate here in the USA. We are regulated. We do follow the laws of the land. We check people's credentials. They give us their social security number, which is a legal requirement. We then check it against multiple databases to ensure that we know who they are. So the suggestion that we are not actually really following and being very careful about the know-your-customer principles is not accurate. But I think it is important that we do know how to run this business in a way that protects consumers here in the USA already.

SENATOR WRIGHT: But where you were going, if you're currently in California player poker and gambling, that's illegal.

SENATOR NEGRETE McLEOD: That's illegal?

SENATOR WRIGHT: Yeah. I mean, today. So these gentlemen, like his site, blocks you when you try to go into play. He primarily in the U.S. does horseracing which is currently legal. So if you're playing poker today in California or probably in most places in the United States, you're doing so illegal. The fact

that you're playing online right now means that you're doing something that's under the table.

SENATOR NEGRETE McLEOD: Do you think most of the people recognize, are cognizant of the fact, that they're illegal? Do you think a lot of naïve people, you know, are playing and not knowing?

SENATOR WRIGHT: Earlier, in Washington, it's actually a felony if you get busted. And in other states, what you run the risk of is, they can confiscate the money. They're not out trying to arrest people for playing as much but the IRS can and, on occasion, does confiscate the money. So the risk that you have, that you've heard them describe a little bit earlier, is that you can win a pot and then not get your money.

SENATOR NEGRETE McLEOD: Not collect because...

SENATOR WRIGHT: Because your risk is that now it's trying to transfer this ill-gotten game to you in a way that doesn't get them busted—so there's kind of a circuitous route sometimes to get the cash back to you.

SENATOR NEGRETE McLEOD: So do the police departments have a vice unit that takes care of illegal stuff, illegal gambling stuff?

MR. PAINTER: The problem is, most of these sites, Senator, are outside of the country and outside of its jurisdiction.

SENATOR NEGRETE McLEOD: Okay. So they can't prosecute them; they can't go after them?

MR. PAINTER: That's right.

MR. SAVIO: I think it's important to emphasize, that when/if California state comes up with a solution and regulate it and make it safe and so on, there would still be offshore sites. I mean, it's not going to work in another way. To do our job, our job, the land-based casinos, poker club's job, is to make this a better choice, safer choice, for the players, and I'm sure we can do that. I mean, it has been shown several times in Europe that people actually attend. When we talk about money, sometimes big money, you want to play at a place where you actually know that, at the end of the day, you can cash out and get your money.

Those are the benefits the player doesn't have today. They really rely on the trust from those sites that are out there today.

SENATOR NEGRETE McLEOD: So...

SENATOR WRIGHT: I think. Go ahead.

SENATOR NEGRETE McLEOD: Is gambling legal—in which nations?

MR. SAVIO: Sweden, for example.

SENATOR NEGRETE McLEOD: Yeah, Sweden.

MR. SAVIO: It's regulated and it's state driven. And due to the fact that EMC ?? has a slightly different point of view on what you can do and not do, there are companies from UK, other countries, doing advertising in Sweden. So the Svenska Spel, the Swedish authority, they are fighting on the same premises as you will be fighting. Maybe the difference is that those other sites are even more legal than the offshore sites will be here, but there will always be the two different choices.

So it's up to you, us, and your colleagues here to determine how we can set the playground which will make the players decide to actually play on the regulated sites.

MR. BARRY: I think the obvious comparison is Italy where, you know, they've slowly introduced legalized poker. They started with tournament and with the introduction of cash games. It's estimated by the end of this year, 80 percent of Italians will play on a legal site. And that's gone from naught to 80 in two years.

The other issue about identifying sites, most of the regulated sites will have symbols or seals at the bottom of the site which will indicate that they're regulated, who they're regulated by, and who you can challenge. And, you know, sites will put up bonds to protect player funds, and you can go to the regulator and go, give me my money; they didn't give it to me. And it would be incumbent upon the regulator, which would be funded by the industry, to promote such a symbol so that it is easy for people to identify what is a regulated site and what is an illegal site, and that will make it much easier for the customer to make the right and the safe choice.

SENATOR WRIGHT: And the confusion, a little bit earlier, Senator Negrete McLeod, was that the bogie, the number you were trying to get in Sweden was about a third of the people who play came from the offshore sites to the state-run site.

MR. SAVIO: Correct.

SENATOR WRIGHT: The Italian model is the 80 percent where they captured in all gaming combined, not just poker but in all online gaming, they've captured 80 percent. There was a bit of confusion earlier about the 80 versus the 30. The Swedes got to 30 in a primarily poker environment. They've gotten to close to 80 in an online gambling environment.

MR. BARRY: And the difference is that Sweden went for a state monopoly.

SENATOR WRIGHT: Right.

MR. BARRY: And that Italy has allowed an open, competitive market which has allowed the experts who know what they're doing to come into the market to invest in product and marketing and inundation ?? of people, and they know how to challenge the offshore operators. They know how to develop the appealing product; they know how to do payments; they know how to do customer service; and, you know, they back themselves to take it on—whereas a state monopoly doesn't have those same incentives and there isn't competition to drive that body. So, you know, that's quite....

SENATOR WRIGHT: Roberto.

MR. SAVIO: I think the point from the Sweden perspective, we thought 30 percent, which you correctly stated in the beginning of the day. Thirty percent of something is much more than a hundred percent of nothing, right? I think the problem in Sweden is that the authority is not going after those companies big enough. As Jonas said, there are ads every day in every newspaper from almost every site of the big 20 in the Swedish paper, which is completely legal.

There is right now a court coming up where they're going to charge or try to charge a few of those magazines, newspapers, and we will see what the outcome will be. But if the state is really following through and going off with those guys, I'm sure we would have seen 45 or 50 percent of the market actually going over to the regulated site.

So in our case, that is a big part of what people easily do to marketing and other still are playing on the other sides.

SENATOR WRIGHT: Okay. Gentlemen, thank you so much and thank you for coming from Melbourne.

MR. BARRY: My pleasure.

SENATOR WRIGHT: The site of the Olympics in '56, I think.

MR. BARRY: Fifty-six. An Irishman won a Gold Medal. That's how I know.
(Laughter) That's a rare occurrence. Ronny Delaney, 1,500 meters.

SENATOR WRIGHT: Wilma Rudolph ran in Melbourne as well. Wilma was sister from Tennessee who ran the one and the two. Yeah, she passed away.

SENATOR NEGRETE McLEOD: I didn't know you were related to her.
(Laughter)

SENATOR WRIGHT: See, we're all related. It's 6 degrees of separation.
But thank you so much for traveling.

MR. BUTLER: Thank you very much.

MR. SAVIO: Thank you.

UNIDENTIFIED SPEAKER: Thank you.

SENATOR WRIGHT: We're going to keep going to the player's panel.

Okay. Don't be shy. Come step right up there. Okay.

Hi. Welcome aboard. John, you're first up. John of the Poker Players Alliance. Welcome aboard, sir.

MR. JOHN A. PAPPAS: Thank you, Mr. Chairman. I appreciate the opportunity to speak to the committee today.

My name is John Pappas. I'm the executive director of the Poker Players Alliance. The Poker Players Alliance is the one and only grassroots advocacy organization for poker players who represent approximately 1.2 million Americans who play poker online, in casinos, in card rooms, or at their own kitchen table. We also, here in California, represent 127,255 members of the Poker Players Alliance. These people live in your congressional districts or your Senate districts. They shop at your grocery stores; they go to school with your family members and they're also you're voters.

It's important to note that in California and across America there's an estimated 1 million in California and about 15 to 16 million online poker players so there were some numbers batted today, about 16 million online pokers in California. That is certainly not the case. That is a wildly exaggerated number which would be remarkable if that was the case but it's not.

It's not surprising, though, that poker has become a phenomenon, particularly here in California. The game was brought here during the Gold Rush, and it epitomizes the competitive nature and frontier spirit of the people who've traveled west from new opportunity. And, you know, the game has now really evolved over the centuries. Where it was once played only on the felt table, it's now being played on the computer table, and I think it's commendable that this committee is taking time to address this new and emerging platform. And from the player's perspective, I just want to thank you for taking the time and also say that ultimately what the committee needs to consider is, despite all the corporate interests and gaming interests in the state, that you need to consider the interests of the consumer. The consumer is ultimately the one who's going to make this a successful model or a failure. Without addressing and looking at what the concerns of the consumer is, this will just be all for not.

A couple of other misconceptions that were thrown out earlier that I feel I needed to address was, one of the facts that playing online poker is illegal. It is not illegal and not even arguably illegal here in California for someone to play online poker. There is no state law which says that—in fact, there's no federal law—which says playing online poker is illegal. So let's just take that discussion off the table.

The PPA has been fighting in Washington, D.C., for licensing and regulation of Internet gaming and Internet poker specifically in two specific bills—HR 2267 and S. 1597 which both give California and the tribes unfettered choice to participate in the federal system. It would allow residents to play in nationwide, if not global, network. And then the states can also collect revenue from that. In fact, looking at the Senate model, S. 1597, it is estimated that California could reap about \$1.3 billion over ten years from the 5 percent deposit tax that is proposed in that legislation. The state can also choose to opt out and do, as you guys were discussing today, create an Internet system.

Again, I think the only thing that we would have to say about that is that we prefer the federal model. We believe it's a better option for the consumer. But if California does go down that path, it must be a competitive marketplace. It cannot be limited to a single tribe, a single card room, or a single player. There needs to

be an open licensing system where multiple people can compete for those licenses. This not only will generate, we think, the ultimate consumer experience in terms of choice and opportunity but also it creates an innovation and a variety of choices for the player that is not available under a monopoly system.

The cornerstone of the system here is the idea that this is a build-it-and-they-will-come opportunity. This field-of-dreams notion is not going to work here. The idea that California can just put up an online poker site and players will just naturally gravitate to it is not going to work. They're going to have to compete with the offshore unregulated sites, and I think the more natural position would be for the state to find a way to naturalize, normalize the existing offshore sites to be regulated here, expand the marketplace to include the tribes, the card rooms, the Googles, the Yahoos, whoever else wants to compete in this marketplace, and have a real robust system that creates the widest range of revenue for the state.

With that, I had written remarks here that I don't want to go into. They were provided to the committee. I would like to defer to my colleague and in-state resident and state director for the California Poker Players Alliance, Steve Miller.

MR. STEVEN J. MILLER: Hello. My name is Steve Miller. I am a resident of Los Angeles. I do serve as the California state director for the Poker Players Alliance. There are over 1.2 million members at the national level and over 125,000 registered members of the Poker Player's Alliance in the state of California.

We've heard from a lot of interesting people today, from all facets of this business, very educational and informative to me as I'm sure it was to you as well. But I speak to you today as an online poker player. And so far, for seven hours, we haven't heard from my type of person. I'm the guy that plays, I think it's my interests that you're looking out for when you decide, if you decide, to regulate poker, online poker, in the state. I also speak to you as a California citizen that is concerned about the amount of tax revenue that's available to the state which is now flowing out of the state.

There are clearly a variety of choices today for the California online player to play the game of poker and I think, that if the state were to move to a state-controlled monopoly environment, there's likely, as we heard about in the Swedish

system, likely see quite a few people experiment, dip their toes into the water, see what the cite is like, but the issue will become one of retaining that player, and it's a business that currently is populated by world-class companies with world-class marketers. They're the Proctor and Gamble equivalence in the online gambling world. The players who play these sites are very strongly brand loyal to the sites that they play. As John said, I don't, I also don't agree with the field-of-dreams assumption, that if you build it, it will come. They may come and visit, but I don't think they're going to come and stay.

The choices that are available to the online player in California today know that the companies that they deal with understand their customers' needs. They respond to those needs with excellent customer service; they provide a safe environment to play; they continually strive to innovate their product to make the game fresh for the player and provide a variety of economic benefits and low cost for the players to play the game. It's been clear in many different studies that poker is among the stickiest type of content today on the web, and it's my opinion that the vast majority of players that will continue to play in the state of California, assuming that poker is available as a regulated site ___ play, will continue to play on the site that they're on.

In conclusion, I think, that in order that the interests of the online poker player in California continue to be best served, the companies that compete should provide a variety of games at a variety of different monetary levels using a variety of different structures, continuing innovation of the game, permit the player to do so in a safe environment, working with a company that they trust; that trust is established over time—it's not a given—and with whom they trust their money with, an opportunity to—it's afforded through a competitive marketplace to keep the transaction costs low to the player and keep the economic player benefits high. And if these player needs are met and if a competitive market environment is permitted in the state, I think that this is the best way to deliver the most amount of players to the state which will result in the maximum tax revenue at the highest potential value to the state of California.

Thank you very much.

MS. MELANIE BRENNER: Thank you. I'll keep this short and sweet. Poker Voters of America is a nonprofit organization whose mission is to advocate for the strongest possible consumer protections for online poker players.

For the past several years, poker voters of America has provided information, resources, and expertise to state governments seeking to design and implement such safe regulated online poker systems. On behalf of the current online players in the state of California, we thank this committee for its efforts. It's been a long day. You've had a lot to listen to, but we really appreciate your time.

We offer our resources and cooperation to the members, to tribal compact holders, and state licensees in order to help craft appropriate and fair legislation. We believe that such legislation must conform to a federal law, create a legal, regulated and sustainable online poker model that also protects current land-based gaming licensees and compact holders. Safeguards to California players by offering legal, secure, and regulated alternatives to unregulated, foreign, online poker incorporates input from California citizens, law enforcement, and gaming experts to ensure that California's legal intrastate sites are competitive and economically viable, allows the fastest possible startup time for a California intrastate online operation, and generates the highest level of revenue for the state. Thank you.

SENATOR WRIGHT: We might have a split. Our California—and maybe I'm off here—but I was just double checking. We recognize four places where you can play poker—in a card room, in a tribal casino, at a charitable event, or at a friend's house.

MR. PAPPAS: Or in your own home.

SENATOR WRIGHT: Huh?

MR. PAPPAS: Or in your own home.

SENATOR WRIGHT: Yeah. When I say *friend's house*, yeah, but in your own home, but there's no profit being extended. If you're playing online poker, it's at profitable venue that is not one of those four. So how do you...

MR. PAPPAS: Well, you are playing in your own home, but it's the "criminal activity" and I put that in quotes, is not conducted by the player themselves. The player is not engaged in the business of betting or wagering. The player

themselves is simply playing a game with other like-minded individuals over the Internet.

SENATOR WRIGHT: But when the IRS confiscates the money, then they were acting illegally?

MR. PAPPAS: If the IRS confiscated money of Internet poker players...

SENATOR WRIGHT: Which they have done.

MR. PAPPAS: The IRS, as far as I'm aware, the IRS has never confiscated money. DOJ has confiscated money, and the PPA is in the process of trying to litigate that money back for the players.

SENATOR WRIGHT: When I say IRS, I misspoke. But the government has confiscated people's money who were playing Internet poker.

MR. PAPPAS: Correct. But generally the money has been confiscated from an online payment processor who is also conducting other activities, not just poker.

SENATOR WRIGHT: But if you were playing, that's kind of like, whatever you call it, that matter, if my money's gone, my money's gone. I know in one instance...

MR. PAPPAS: Regardless of, I think, the consumer's better served from a licensed and regulated environment, without question, in which there was a clear path for their transactions to go to and from the online site and that is something that is not in place today and would be a significant benefit to whether a federal model, which the PPA supports, or a state model which you guys are advocating today.

SENATOR WRIGHT: We would agree there because I know the federal government also, as we heard earlier, but the tag on the credit cards was strong enough to make both VISA and MasterCard not even let you play with them any more, from a U.S.-playing standpoint, but the same drill. I mean, I don't know that anybody's ever been arrested for playing but it's a felony in Washington by state law.

MR. PAPPAS: Yeah, it is a felony. Washington State's the only state in which it is a felony.

SENATOR WRIGHT: Okay. Do you believe that, if we were to make California, or if there was a federal site, that the lack of risk of your capital would make the game more attractive?

Steve, you play a lot. Would that, would you change to the California game if it were available tomorrow and you didn't feel you had any risk of your cash? What would California have to do to entice you to switch?

MR. MILLER: Well, first, let me clarify, I do not play a lot. I play occasionally online. (Laughter) It's true.

SENATOR WRIGHT: He put the handcuffs down. You're okay.

MR. MILLER: Is he still here? I can't see. (Laughter) Without a doubt, without a doubt, the more consumer protection that I had would certainly be one of those key benefits that I would look to, to make my decision as to where I wanted to play. I assume that the companies that we just heard from, they currently have those types of systems in place. And I also assume other companies that aren't represented today, should they choose to also participate in the California marketplace, would also implement that type of consumer protection system.

MR. PAPPAS: I would add that, you know, given that there's a million players, estimated million players, online today, the Wild West is probably not the best way to describe the marketplace. There are those who are—none of the operators are licensed here in California—that is correct—but there are licensed and regulated operators from very reputable jurisdictions across the world that are taking play from California residents, and California residents feel very safe playing on those sites. They put their money on; they get their money off. That's why there is a robust marketplace here. But I do believe there would be an opportunity for an even larger and stronger marketplace, should California or the federal government make the decision to license and regulate it.

SENATOR WRIGHT: And as I mentioned earlier, I'm going to go to Senator Harman. But one of the offshore sites actually reimbursed the people who had their money confiscated, with interest. So I mean, to your point, that really restored the confidence when the company came back and said, you know, I know this happened, sorry.

MR. MILLER: Senator, that actually happened to me in June of 2009.

SENATOR WRIGHT: He just picked up the handcuffs. (Laughter)

MR. MILLER: I believe that at the time, there were approximately 27,000 accounts of players across the nation which were frozen. And the operator that I worked with stepped up to the plate and wanted to keep me as a satisfied customer, added a 10 percent bonus to the amount that I was due, and immediately cut me a check from a commercial bank located in Canada, and I was satisfied.

SENATOR WRIGHT: I'm so glad you said that because, see, those people were saying he made that stuff up, so I'm glad you were there.

MR. PAPPAS: Certainly, and the PPA is seeking a venue in which to get that money back for the players and to be able to challenge that they were not engaged in any unlawful activity. Therefore, the money should never have been frozen or seized in the first place.

SENATOR WRIGHT: Senator Harman.

SENATOR HARMAN: Thank you very much, Mr. Chairman.

I wanted to ask Mr. Cunningham about—excuse me—I got the wrong one. I want to get Mr. Pappas. Thank you.

Mr. Pappas, we've heard testimony today about the offshore activities or unlicensed, unregulated, consumers are at risk, it's underground, all of those things. And it seems like many of the speakers have indicated today that if some type of plan were adopted here in California that it would be a plan that should protect consumers more. And my question is, How widespread is it with these offshore operators that there's some type of—well, I'll use the word *shenanigans*, not a very good description, but cheating, fraud? There's, you know, all types of different—how often does that happen? Can you quantify that? Is it really rampant in the industry, or is it just—we've heard the illustration of the gentleman from California that he did have an incident and was reimbursed for it. But how often is this happening?

MR. PAPPAS: To be clear, this incident wasn't anything with the site. It was actually with our misinterpretation of our government and misinterpreting

the laws that seize the funds. That wasn't anything that the site had done, perpetrated. It is not rampant.

SENATOR HARMAN: But when I think about the consumer protection, I'm thinking somebody is cheating the consumer. They've figured out a way to, you know, cheat me if I played. I'm not a very good poker player. It would be pretty easy to cheat me, I'm sure, but how often does that happen?

MR. PAPPAS: Not as often as has been perpetrated here. Again, to be clear, most of the sites that operate and take place from the U.S. are licensed and regulated in reputable jurisdictions, like the United Kingdom, Alderney, Isle of Man, Gibraltar, Italy, places like this. They are licensed and regulated. They are not licensed and regulated here and we would have believed that additional regulation, either applied by the federal government or here in the state of California would give the consumer even greater confidence to continue to play online. But we wouldn't have the marketplace that we have today and the marketplace wouldn't be growing as it is today if this was just an industry full of swindlers.

People aren't going to put their money online and not get their money back...

SENATOR HARMAN: Exactly.

MR. PAPPAS: ...and continue to do this.

SENATOR HARMAN: Exactly.

MR. PAPPAS: And human nature would not allow that marketplace to exist. This is an industry built on trust, and the largest operators that are operating today are very trustworthy and they have brand loyalty, and the players enjoy playing on those sites and they want to continue to play on those sites. And those sites would like to be licensed and regulated here in California along with the other gentlemen that were here on the panel earlier, as well as other, the card rooms and the tribes and, you know, who knows, the Googles and Yahoos of the world that might also want to enter this space.

SENATOR HARMAN: Thank you, Mr. Pappas.

MS. BRENNER: I was just going to say, when we started our efforts here in California, we started in the Attorney General's Office and asked them if they were

getting complaints, and they said that they did get complaints, hundreds of complaints, every month. Now some of them weren't relevant. Somebody would say something like, hey, I had a pair of kings. How could I get beat? But the problem was, when they said, what can we do about it, they had to say, don't play. So there wasn't anything; they had no recourse. And I do strongly believe that there are a lot of people out there that play at subscription sites. A couple of my friends in particular who would look at moving to a site if it was regulated, and we do believe that we would actually grow the number of players in California if we had a regulated system.

SENATOR WRIGHT: Okay. Thank you for this panel. If, I guess, on the way, the last question, guess as a percentage, if we take Sweden as one bogie at 30 percent, different from Italy, but Italy won ?? 80 percent, but Italy also had more sites. What would you estimate to be the, what California could expect to receive as a percentage of the people who already play?

MR. PAPPAS: Well, I think you can receive 100 percent of the play if California does it in this manner: First, finds a path of normalization for the sites that are currently operating and have the liquidity and allows new entrants—that includes the card clubs, the tribal casinos. There would be no reason for a player to play on any other site but those that were licensed here in the state.

SENATOR WRIGHT: You think it's—and I guess anything is possible—so you think it would be possible to create an agreement, say, with the Isle of Man, so that a California player who played on the Isle of Man site, that the Isle of Man would send us a check?

MR. PAPPAS: The agreement would be through any of the deposits made by California players would either be taxed or however you guys want to build your tax structure. It's not for me to decide. But the tax structure would be built so that any deposits made by California players would be segregated and their winnings would be segregated and the individuals would be required to pay income, state, federal income tax on those, as well as whatever tax the company would have to pay for...

SENATOR WRIGHT: That would be a fairly complicated scheme. I mean, there are 50 states. And if every state had its own taxing regimen, I think the Isle-

of-Man guy would say, You know what? I'm just going to keep doing what I'm doing because I'm already getting a cow. Why do I want to—you know, I'm already getting the milk. Why do I want to buy a cow?

MR. PAPPAS: Again, that's why we would advocate, and we have been advocating, not for a piecemeal approach, where each individual state looks at this but, rather, a federal model in where states could opt in or opt out of that system and I think that would create probably the greatest benefit not only for the consumer because they would be able to play under a marketplace with all U.S. players and the world. Under a California system right now, what would be proposed, if there was intrastate poker, if I'm a poker player in California and I go online today, I can play with people in Chicago and Florida and Manila and Italy and across the globe right now, I can play with people.

Tomorrow, if there was to be a closed intrastate California marketplace, the consumer would only be able to play with other California players. From a consumer perspective, that is a lessening of choice, a lessening of whatever games that they would like to play. Right now, they can go on and find a game at any hour of the day. That would not be the case under a limited California marketplace, so that is why we advocate for the federal model which would allow for Californians to play with people across the world, not just within their own borders.

SENATOR WRIGHT: Okay. All right. Thank you all so much for coming, and your testimony that you've written, and we'll keep looking at it.

MR. PAPPAS: Thank you.

SENATOR WRIGHT: The horseracing panel. Mr. Fravel, welcome aboard.

I'm going to—is Mr. London here? Oh, I didn't see you there. Carl, if you—I'm just going to just put just two folks up at the same time, just to...

UNIDENTIFIED SPEAKER: _____.

SENATOR WRIGHT: I didn't want you to be there by yourself.

UNIDENTIFIED SPEAKER: _____.

SENATOR WRIGHT: I'm going to take the horseracing first.

Mr. London, if you'd just be there, we'll go right to the charities.

MR. CRAIG FRAVEL: Mr. Chairman, Craig Fravel of the California Horseracing Alliance.

I've been sitting here thinking all day that I'm waiting for Captain Reno ?? to leave Rick's American Café and say that I'm shocked that there's gambling going on here.

SENATOR WRIGHT: It's amazing, isn't it?

MR. FRAVEL: It is; it is amazing. And I also wanted to say, I agree with the Indian tribes. Now what that means exactly is not entirely clear at this point because there is obviously no proposal on the table so we're not here to...

SENATOR WRIGHT: Let me further—which tribes? (Laughter)

MR. FRAVEL: Exactly. So I'm not here to oppose or support any particular proposals, but I am here partly to defend an exclusive, if you will, just much like the tribes have a very legitimate concern about their exclusivity arrangements and the votes of the people.

Horseracing in California is a sport that dates back to the 1930s, right at the end of the depression, and was the first legal form of gambling in California permitted since the 1800s. And we are actually enshrined in the California Constitution, much like tribal gaming is, and we have a de facto exclusive in terms of Internet wagering, as some of the earlier testimony indicated. There has been Internet wagering going on, on horseracing, since the early 2000s. It has been done both in a highly regulated fashion, in a very responsible fashion, with safeguards to protect the young, and those in need of additional assistance and has been done very successfully at present.

In the past year, there was approximately \$450 million wagered by California residents on horse races from both California and around the United States and some foreign races. And to my knowledge, there has not been one complaint registered or investigated or even considered of anyone underage wagering on horseracing. We've had exceptional enforcement on residency requirements and locations, and an open architecture for regulators to be involved in all aspects of that business.

So I really don't want to use up too much of your time because I know you've been here a long time. But as this discussion moves forward, I think the

interests of California racing are that it be taken into account and be part of this conversation on an ongoing basis; and obviously, you understand, that having invited us to this hearing today and we appreciate that very much.

I will harken back to a degree to the creation of the California Lottery. Several other instances of expansion of gaming and horseracing, partly of its own fault at various times, and other times not by its own doing, were sometimes left out of the conversations, and it's very important to us to be part of this conversation and other gaming conversations because we do have a track record, so to speak, of being a responsible gaming partner with the state of California and a rich history of conducting that to the benefit of California residents.

We also have, represent, over 17,000 workers, perhaps the size, 30,000. The numbers have been declining in recent years, but the economic downturn and a huge economic impact with good jobs for both skilled and unskilled labor and farm workers, open space, and that's an industry that I know you have been involved in helping us, and the legislature has been very receptive to us and we just want to participate constructively in this discussion. Thank you.

SENATOR WRIGHT: Let me make sure I understand. So you would like to see us go into Internet gaming, or you would like to see us not go into Internet gaming?

MR. FRAVEL: Well, horseracing's already in Internet gaming.

SENATOR WRIGHT: Right.

MR. FRAVEL: And to be honest with you, you know, we would like to be able to have the ability to expand the types of wagers that we currently offer and the kinds of activities that we engage in. On that, we don't have any specific proposals for you at this point, but we want to continue to maintain the position we have. And if there are other opportunities, we want to be part of those opportunities.

SENATOR WRIGHT: We'll try this one more time; then I'll shut up. Relative to Internet poker, you would be in favor of the state moving in that direction or you would not be in favor of the state moving...

MR. FRAVEL: I don't think we have a position on the public policy issue of whether the state of California should permit Internet poker. I can tell you that

many of the positions that have been taken earlier about it, it's better to get 100 percent of something—or 30 percent of something than 100 percent of nothing—or the same kind of discussions we had back when we were interested in the expansion of the Internet, and those certainly are worthy of consideration.

SENATOR WRIGHT: Okay. Oh, he's gone.

Okay. Well, Mr. London will move right over.

MR. CARL LONDON: Thank you, Mr. Chairman, should I wait for the other members to come back or do I just start? I'm teasing you.

SENATOR WRIGHT: We'll fill them in when they come in.

MR. LONDON: I'm teasing you. Thank you. I'm here today on behalf of the California Charity Bingo Association, which is a nonprofit organization representing community-based charities, citizen volunteers, and game vendors. The mission of our organization is to preserve and promote bingo games that provide desperately needed funding to important charities throughout California. I want to—the recent activities in this area sort of predate you're coming back to the legislature so I wanted to at least raise for just a moment, you know, a brief history lesson from only a couple of years back, and it was just prior to getting back here.

But Sacramento County is a great snapshot to use for studying the impact and benefit of charitable bingo. In the last couple of years here in Sacramento alone, we've raised approximately \$10 million. These went to all Sacramento-based charities, like Sacramento Society for the Blind, United Cerebral Palsy, Senior Gleaners, which does meals to senior shut-ins, the Capital Freelancers Drum and Bugle Corps, and the booster clubs for seven of eight high schools in the San Juan Unified School District.

Looking around the room today and around the legislature, I know that several people that work in this building—legislators included, some lobbyists—have worked at the charitable bingo halls, and these are exclusively run by volunteers. All of the money, the profit, goes to the charitable organizations represented. The \$9.5 million I represented earlier, basically that's 33 percent of the net take. That's a very high return for any fundraising investment that charities might get involved in. The \$9.5 million has basically occurred while state

and local government budgets obviously have been slashed drastically. And you talked about this in the budget hearing the other day brilliantly, I thought, talking of the choices that we're making. But clearly, we're just blasting away at that safety net. These charities that benefit from charitable bingo are the only string really holding the net together in some cases. Our string recently ran out when legislatures saw fit two years ago in only 11 days to pass a bill that clearly banned electronic bingo.

What I find ironic about the conversation today is that we're discussing the prospect of developing a poker model because it's out there and because we see money there possibly. We know it's a game that's developed and evolved because of electronic things like that have evolved. That's life. And then on the other side of that, you have the argument of exclusivity. Well, in the case of bingo, we just have one very simple appeal to you. Don't forget about the charities and the groups that do this work. It's ironic the position we're in today and the discussion we're having.

I do have to say that this is truly one of the best hearings I think I've seen in a long time, information ____, staff, and you really deserve a lot of credit for that. But in looking at what we're talking about, we're talking about a technological revolution that's provoked this question. And relative to bingo, we've had the same possibility and the same possibility has developed overseas as well. Yet in California, because of mostly tribal interests, we've sought to basically make sure that charitable bingo is stuck playing paper-rock-scissors forever. We've got a paper game. It's not going to be a big moneymaker. You're relegating those groups to that.

So what I'm saying to you is, as you consider the impact of the technological revolution and its impact on gaming and what you might do there, we'd like also the same consideration if you looked at, in terms of what happens with the charities that have a bingo model, let us evolve a little bit. Let us look for a model that tracks with that and recognizes that technology does allow for things to be played at a little faster pace, a more desirable pace, for people who live in this century, and let us do what we can to help backfill the safety net that we've been destroying.

We've got a couple of suggestions along the way, and that one is to look at the possibility of a statewide bingo game. Again, this is done in other countries very successfully. It's often more popular than Lottery because the bingo model, even though you can do it electronically, someone always wins. Lottery, that's not always the case. In bingo, you call the numbers till someone wins so there's always a winner. It makes it very attractive.

The second thing is that we need some kind of fix to the law that was given to us when the legislature—not you—banned electronic bingo, and that is, to fix the remote caller bingo model, if it's ever going to have a chance to work. We've been on record with laying out what our concerns are with that. It's a model that basically allows a closed-circuit version of bingo to be played among organizations that are affiliated and tied together. There's some serious restrictions in there that will make it such that charities will never advance on that.

And the third thing is, if you are going to look at some form of Internet gaming moving forward, we'd urge you to consider looking at some sort of mechanism for a charitable interest to be a part, at least a small part, just to help with that.

There's also a very interesting website. I'd urge you, you and your staff, to look at. It just came across, as someone had mentioned it to me, but it's www.betoncharity.com. It's not ours; I've never seen it before the other day. It's an interesting site where they do an offshore gaming model where they allow you to, for part of the administrative fees you're paying into, to declare which charities you want that to go to. It's an interesting site. Again, I don't know if it's legal or not. I don't want to engage in that discussion, but I just want you along the way to urge people to remember there's some other interests out there that should be allowed to advance as well, and I thank you very much for your time.

SENATOR WRIGHT: Thank you. There won't be questions that you would like us to review the legislation relative to Internet bingo. That would be a thing you would entertain?

MR. FRAVEL: I think it's worth looking at again. You know, if you're looking at other issues that come out of the electronic era, bingo's been successfully turned into a game in other countries, particularly where it's been

quite successful as a revenue generator and government run and done really quite well and benefiting interests designated by the government agencies.

SENATOR WRIGHT: Thank you so much.

We'll move to our last panel—Terri Sue Canale—that's actually a great Italian soup; Reverend James Butler; and Fred Jones.

Thank you for participating with us a good part of the day.

Ms. Canale, welcome aboard. Thank you so much for being here.

MS. TERRI SUE CANALE: Thank you. It's been a nice day. I'm sure everyone is still watching so I'm not worried that they're not.

First, I want to say, I'm encouraged to hear all the testimony previously talk about responsible gambling, talk about problem gambling, and talk about underage gambling.

A couple years back in 2007, Senator Florez had a similar hearing on problem gambling, and what I heard all day was problem gambling—the only problem I have is not winning. So we've come a long way in the state of California. The Office of Problem Gambling was founded only in 2003. Our mission is to provide quality research-driven leadership in prevention, intervention, and treatment for problem and pathological gamblers, their families, and communities.

OPG does not take a stance for or against gambling, and I want to be very clear about that. We don't lobby either way. So I just want to tell you what we do know about California gambling behavior, about Internet gambling in California, and about problem gambling among the Internet gamblers in California.

In 2006, we conducted a prevalence study, and that prevalence study had 7,121 respondents. It was the largest prevalence study done in the United States of America; 1.1 percent of those folks gambled on the Internet in the past year. So how does that equate to a number? If you look, it was only for over 18 years old; it wasn't for any youth; 26.3 million, so a couple of hundred thousand had participated in Internet gambling over the previous year.

Between 1999 and 2006, the past-year participation of Internet gambling increased. We also found that. It also showed that Internet gamblers to be significantly younger than the general population of other gamblers. Almost six out of ten were under 40 years old. The majority of the Internet gamblers, 65

percent, when asked, said that they played—the very last game that they played on the Internet was poker. So the majority of the Internet players in California in 2006 were playing poker.

Additionally, in a 2006 study, it indicated that 3.7 percent of the total population in California, adults suffer from problem and pathological gambling, so close to about a million people. Another 2.2 to 2.7 percent are at risk of becoming problem gamblers.

Now we also fund a toll-free helpline service, 1-800-GAMBLER. And from that—in 2009, 1.8 percent of the callers to the helpline gambled on the Internet. So out of a total of 5,009 callers, about 90 people called in, and they're primary choice of gambling was Internet gambling; 1.6 percent of that 1.8 was cards on the Internet, so there was only a .2 percent difference from cards to other forms of Internet gambling, again, mostly gambling on cards. In addition to that 1.8 percent that that was their primary preference, 3.3 percent indicated that the Internet was their secondary gambling preference. I know that 3.3 percent, 2.9 percent, again, were cards.

We also know that recent California law have included language related to responsible gambling programs, and we talked about that today. There's card room regulations in the California Code of Regulations. And the recent tribal state gaming compacts, section 8.5, also deals with responsible gambling programs.

These programs have posting requirements for the 1-800-GAMBLER number, signs and symptoms or problem gambling, and how to get help. In addition, there are self-exclusion programs, opportunities for problem and pathological gamblers to voluntarily restrict their access to the gambling sites, whether it be brick or mortar or whether it be for Internet, I think that can happen either way, and also securities to eliminate access for underage gamblers. In 2006, the Attorney General's Office report, the *Golden State Report*, states that problem and pathological gamblers present a social cost of nearly \$1 billion annually to the state of California.

So in closing, I think that it's great that you've invited the Office of Problem Gambling here; I think that it's great that everybody is talking about problem and pathological gamblers; and the only thing left is that funding is necessary to the

Office of Problem Gambling to mitigate the problems from pathological gambling. Thank you.

SENATOR WRIGHT: Thank you.

THE REVEREND JAMES BUTLER: Good afternoon...

SENATOR WRIGHT: No, you're good.

REVEREND BUTLER: ...and appreciate the opportunity, Chairman Wright.

In the testimonies that we've had today, it's been pretty clear that there is an expectation that there will be an increase in gamblers and an increase in the dollars spent on gambling. That correlates to an increase in the gambling problems, and I appreciate you being here because I'm one of the people who read your report—great job. In that report, as she pointed out, there's more than 1 million problem and pathological gamblers in California over the age of 21. There's also...

SENATOR WRIGHT: Let me rewind and just have you state your name and where you're from.

REVEREND BUTLER: I'm sorry.

SENATOR WRIGHT: That's okay.

REVEREND BUTLER: My name is Reverend James Butler from the California Coalition Against Gambling Expansion.

Again, the testimony indicates that there will be an increase in gamblers and money spent. That will collate to an increase in the problem gamblers. And, as was pointed out, there are currently more than 1 million problem and pathological gamblers over the age of 21, another 500,000 in the same report that are under the age of 21. And the problems that are associated with this increase will be an increase in crime, increases in unemployment, welfare, bankruptcies, and deteriorating health of the players. There will also be the social costs that include divorce and an increased rate in suicide.

Those social costs are not even calculated into the \$1 billion that gambling is currently costing the state of California. When that number increases, the cost will increase. And in spite of what I think is hope, that there will be an influx of cash, it will not be sufficient to offset the economic and social cost of the problem of pathological gamblers.

There was also a discussion in the testimony earlier today that dealt with displaced dollars. Now displaced dollars are not just dollars that are taken from a brick-and-mortar casino and put onto the Internet gambling site. It is also the displaced discretionary dollar that impacts and affects local businesses as well. There is one study even that indicates, that for every slot machine, it costs one job. Whenever you look at how many slot machines there are in the environment, you will have a corresponding loss of one job per because the money that goes into that slot machine is money that is not being utilized in other entities—small businesses, local entertainment, et cetera.

Also, one of the big questions that has been considered and discussed is the ability to enforce the various regulations, and I would just like to share at this point—I'm not going to read the whole answer; I'll consolidate it. This is a copy of a letter that was submitted to the hearing back in Washington, D.C., on December 3rd. References have been made to that hearing before. This comes from the FBI. The question was asked and then submitted, Does technology exist that could facilitate undetectable manipulation of an online poker game? Short answer, yes. So the idea that these will be completely safe and forthright is, I'm certain to hope, that there is currently now technology that can corrupt that.

Second question: Could technology be used to illicitly transfer or launder money in the guise of innocent participation in an online poker game where the undetectable theft of money from one participant in such a game by others acting in concert; if yes, to what degree? Short answer is, yes. And then it goes on explain how that might happen.

Another question, Do you believe the claims of vendors who say they have technology solutions that would validate the age of a potential player in an online poker game or the physical location beyond a shadow of a doubt? There's a long explanation talking about geo, geo-location, and et cetera, and how that's devised. The short answer is, no. In fact, it says it becomes exponentially less accurate when you expand the imminent protocol addressed based on information. In other words, they might be able to tell the country; but as they get finer tuned to states or particular geographical locations within a state, it becomes more and more

difficult to do that. Those are just some of the questions that were addressed in terms of enforcement.

I'd also like to share a recommendation that was found in a report by the National Gambling Commission that addressed the concerns of Internet gambling, especially when studies, many studies, seem to indicate that Internet poker players, perhaps because of their age, perhaps because of the environment in which they play, which is less socially supervised, seem to have a higher susceptibility for problem and pathological gambling. And so the recommendations from this national gambling commission concludes that states should prohibit exemptions or expansions of Internet gambling. And further, in acknowledgement of these potential problems, it also recommends that states not permit the expansion of gambling into homes through technology, i.e., the Internet.

One of the concerns that our organization has, and I imagine you would have as well as you look at the people of California, are we unleashing a monster in their own home, that people who heretofore need to at least travel to a site in order to gamble now can wake up in the middle of the night, find a game, and lose their money. One adage that I used in a letter that I wrote—and I think it may not be wholly original, but we will through the Internet be developing the ability for someone to lose their house without ever leaving home, and I'm not certain that that is in the public benefit of the people of California.

Finally, I do want to conclude, you've made a statement that this an underperforming asset, and I would argue that instead it's simply an illegal activity. Thank you.

MR. FRED JONES: Mr. Fred, Fred Jones, also CCAGE. Oh, there we go. Mr. Chair, Fred Jones, California Coalition Against Gambling Expansion here to answer questions as one of the many attorneys with many differing opinions. If you need, clearly poker is a controlled game. The Penal Code section 337(j) defines what controlled games are. Poker is listed expressly as it. And the only exception to playing at home is, games played with cards—and that's a key phrase—with cards—in private homes or residences in which no person makes money for operating the game except as a player. So I think your summary of the

appropriate legal venues of playing online poker is accurate. And so players that are playing online poker in California right now are in violation of the law. It's even more clear about those that are operating these type of games online.

And so when you ask question, Should we do nothing?, the answer is no. Look at Washington; look at some other states. I mean, a quarter of a billion dollars is not chump change, and that's just the state of Washington. And you heard from the AG's representative that this money is still caged in U.S. banks. So money is still out there for the illegal activity, which again, as Jim said, we do not consider an illegal activity an asset. If that's the case, then prostitution, child pornography, illicit drug sales—those could also be considered assets that we ought to get our fair share of.

So for those reasons but also other, bunch of legal concerns, CCAGE is strongly opposed to the idea of making homes casinos. Thank you.

SENATOR WRIGHT: I think, a couple of things, since I'm by myself, I was born in Chicago. And before they had lotteries, everybody in the south side if Chicago was involved in a numbers business. My uncle in Detroit was actually one of the biggest numbers brokers in the city of Detroit and the fact that—you know, it was interesting because, to be a runner at numbers, for example, you didn't carry paper so you had to virtually remember all of the bets that were placed and reimburse all the people. I mean, there was a whole system that was developed. And when they did lotteries, ostensibly, it was done to break what were then black numbers operations in the Midwest and on the East Coast.

The concern that I'm looking at this as an asset—and actually you could look at virtually anything and you have to make a value decision to your point as to whether or not it's something that you want to engage in. I don't know that we're going to get the train back in the house relative to Internet poker. So the question is not before us, should people do it or not. We can go to where you said, and the AG mentioned, maybe we take the Washington model. I'll bet you the people of Washington, they'll get that money one time, maybe twice, because the sites will morph and they ain't going to deposit in the banks any more, and then your enforcement mechanism is, Can you collect the money? At some point, we would have an expression in South Central, that it's all about the Benjamins. And

so we will move the Benjamins to a place that you can't get them. And just as you heard earlier, many of the sites reimburse the people who lost money. So even in that Washington example, the sites just figured that that was a cost to doing business. Washington got the money; they relocated out of Washington and the thing still happened.

And, Reverend, to your point, I would say it's a question of, if it's going to happen—it's not a question of is it going to happen because we legalize it or not—it is happening; it will happen. I mean, in California, we all know that they don't have sex in prison, and I'm glad that they don't because there would be all kinds of diseases that would accrue if people were having sex in prison. But thank God it's illegal and people don't do it.

But the question I think we have to face here is that we have voted by Constitution that we're going to have gambling. The people have voted on that. We have local governments who have done that. And I think you're right—are there some consequences? You know, Ms. Canale—I love to say that—it's a great suit, by the way. I don't know if you've ever seen the canalis. It ends with an "i" but that's okay. But the canali makes a great soup.

I mean, I acknowledge that there are issues that are associated with gambling, but it's also something that's going to occur. Whether or not it occurs because people just do it on the street, whether or not it occurs because we control it, or whether or not we, you know, launch full scale and prosecute it becomes another discussion. I mean, I would hazard a guess—and there have been studies that have differed on this point—is that probably one of the more colossal failures in law enforcement that we ever had has been the war on drugs. And if I took the progression of that and look at how badly that was botched and I look at what we spend and our result versus those countries that have a far more lenient point of view, they have less drug use and far less carnage than we do in the United States on a similar thing. I mean, you would think the French would be all drunks, but their alcoholism rate is lower than that of the United States.

Go ahead.

MR. JONES: Well, I'll just respond to that real briefly. There's a real interesting misnomer—and I don't want to get too far a field—that somehow the

Europeans, because they have a more liberal drinking policy and younger age, have less problems. Their binge drinking rate is higher than the United States, and there's very few countries in Europe that they're binge drinking, which is problem drinking, is less than.

But back to your other issue here—and I can give you the document, if you want on that—but back to this issue here, even on the example that you had on numbers in Chicago, then they legalize and have a lottery, which undercut, of course, the illegal activity.

SENATOR WRIGHT: They put the brothers out of business.

MR. JONES: But do you think there are at the present time more or less lottery gamblers in Illinois and Chicago than prior to? My guess is that there is more. And with the increased gambler—both number and perhaps the amount—there is going to be a corresponding increase in the problems.

It's an interesting thing, in terms of California studies of the Lottery, is the Lottery is disproportionately burdensome to the lower economic, inner-city, urban, ethnic groups. They are the ones who disproportionate spend more on the Lottery than the average Californian. Now anything you do to therefore increase the Lottery will actually make their burden greater, not lighter.

Now on the Internet poker world, the burden seems to fall on the groups between 18 and 25. They are the predominant players. They are also, because of their age, most susceptible to developing problem and pathological gambling issues. And because of that, you're right, that this may take place regardless of what you or I may choose. However, I'm not certain that the state should be a facilitator in perhaps the destruction of both individuals and families. It is not some sort of a—what we said earlier is that this is how people choose to spend their own money in their own private way and nothing happens. That's great if perhaps you're a hermit and you have no other contact. We live in a social world. And a problem or pathological gambler will impact those beyond them—him- or herself. It will impact family; it will impact friends; it will impact business, communities, and ultimately the society suffers. I would say it would become more course as we expand the opportunities of gambling. And whenever you bring it from a tribal casino—I will say we were able to be consistent—our organization

posed that as well—but whenever you expand that gambling opportunity into a home—and the speculation I read at one point is that currently there is about 75 percent of the California adult population with easy access to computer and Internet. That is a huge, a huge opportunity that we are putting into people’s homes. Someone, if they have an Internet, they have a computer, whether it be a family, an individual, there’s little opportunity to provide the kind of true safeguards—and I think we will beat the world with. I think you can say, well, yeah, there may be some money that can be captured from this opportunity. Even the monies that were being speculated—and it ranged; the numbers were all over the map—one said maybe \$150 million in five years, start 30, 50, and work up, that the state would capture.

How many more problem and pathological gamblers are we going to create? We already have over a billion dollars that this is direct cost without the social element, and we’re just going to be adding to that number; \$150 million is going to be miniscule. And what’s going to finally happen is, the only winners in this are going to be the Internet poker operators. The state will lose and certainly the individuals will lose. The people of California will be the big losers in this, and I think that we have the opportunity to say, you know, there’s another approach to take. Yes, I can do this and do that and capture some money for the state of California, but sometimes there’s something more important. When you look at the cost benefit analysis, not just fiscal impact but cost to benefit, you’re going to say, there is not enough, not nearly enough benefit, to cover the cost. And we simply can’t afford to keep burning that kind of money.

SENATOR WRIGHT: Thank you so much.

Public comment?

MS. CANALE: I agree on the canali soup, by the way. (Laughter)

MR. JOHN STATHIS: For public comment, speak right here?

UNIDENTIFIED SPEAKER: Yes, please.

MR. STATHIS: Should I wait for the chairman?

UNIDENTIFIED SPEAKER: Go ahead and state your name.

MR. STATHIS: Well, we're on the California channel, so I'm speaking to teachers. My name is John Stathis and a retired postal worker living in the San Francisco Bay Area.

California's public school teachers should be the exclusive recipient of the profits from the intrastate Internet poker, if enacted. California should cut out the middleman and monopolize Internet poker to reap the maximum profit for the teachers. The teachers are in a world of hurt, with layoffs and budget cuts, to school districts approved by Governor Arnold Schwarzenegger.

The California Gambling Control Commission is capable of overseeing Internet poker, as it does now with Internet horseracing disputes, instead of tribes. The hard work by our teachers produce the future of our children, and the future of Internet poker should fold its hand right here at the Senate committee if education is not fully funded in authorization of Internet poker in California. Thank you.

SENATOR WRIGHT: Okay. Thank you.

MS. CAROLYN VEAL-HUNTER: Mr. Chair, Carolyn Veal-Hunter on behalf of Shingle Springs Band of Miwok Indians.

I want to reiterate some of the points that you heard earlier today from some of the tribes that oppose the Internet poker of Shingle Springs on behalf of them, opposes as well, for three primary reasons.

One, we are concerned about the economic impacts specifically on the Shingle Springs tribe and its new facility to Red Hawk Casino.

Secondly, we're opposed for the overall impact to all existing gaming tribes.

Finally, we just are concerned about expanding gaming beyond existing tribal lands, especially with respect to exclusivity arguments that you've talked about so much earlier today. Thank you.

SENATOR WRIGHT: Thank you.

Are there any other public comment?

Well, let me—those of you who have been here with us all day, you're really troopers or you really don't have lives. (Laughter) But with that, thank you again all for the participation. I think we really got some good information. There'll

probably be an Assembly hearing similar that will pick up with some of the issues that were raised here and go forward. But with that, we're going to be adjourned.

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