

January 8, 2004

Hon. Bill Lockyer  
Attorney General  
1300 I Street, 17<sup>th</sup> Floor  
Sacramento, California 95814

Attention: Ms. Tricia Knight  
Initiative Coordinator

Dear Attorney General Lockyer:

Pursuant to Elections Code Section 9005, we have reviewed the proposed initiative entitled "The Gaming Revenue Act of 2004" (File No. SA2003RF0059).

## Background

The California Constitution and state law limit the types of legal gambling that can occur in California. Under current law, wagering on horse races and specified games in licensed card rooms is allowed. In addition, Indian tribes with tribal-state gaming compacts are authorized to operate slot machines and other casino-style gaming in California.

**Card Rooms.** The state allows card rooms to conduct certain "non-banked" card games. These are games where the card room operator has no stake in the outcome of the game. The players play against each other and pay the card room a fee for the use of the facilities. Typical card games include draw poker, 7-card stud, and poker pai gow. State law specifically prohibits certain games—such as twenty-one. Current law limits the expansion of both the number of card rooms and the size of existing card rooms until January 2010.

**Horse Racing.** The California Horse Racing Board (CHRB) is responsible for regulating horse racing in California. The CHRB issues licenses to racing associations that then lease tracks for the duration of racing events. In California, there are a total of 6 privately owned race tracks, 9 racing fairs, and 20 simulcast-only facilities. (These latter facilities do not have live racing; instead, they allow betting on televised races occurring elsewhere in the world.) The state receives revenue from the horse racing activities from license fees, penalties, and the collection of approximately 1 percent of the gross amount wagered at any licensed event.

***Gambling on Indian Land.*** The federal Indian Gaming Regulatory Act of 1988 and the State Constitution govern gambling operations on Indian land. Those tribes that enter a tribal-state compact may operate slot machines (up to 2,000 each) and engage in banked card games, such as twenty-one. Currently, 61 tribes have tribal-state gaming compacts and operate 50 casinos with 54,000 slot machines. As sovereign nations, tribes are largely exempt from state taxes and laws, including California environmental and workplace laws.

***Revenue Sharing Trust Fund.*** Under current law, tribes operating gaming machines make payments (an amount dependant on the number of machines in operation) to the Revenue Sharing Trust Fund (RSTF). These funds are distributed annually to each non-compact tribe in the amount of either \$1.1 million or an equal share of the funds should there be insufficient monies for the full payment. A noncompact tribe is defined by the compacts as a federally recognized tribe that either does not operate slot machines or is operating fewer than 350 machines.

***Gambling Regulation in California.*** Under current law, state regulation of gambling, with the exception of activities regulated by CHRB, is the responsibility of the California Gambling Control Commission (CGCC) and the Division of Gambling Control in the Attorney General's Office. These entities are responsible for the licensing of owners and most employees, investigating suspected violations of the Gambling Control Act, and assessing fines for violations of state law. The CGCC is also charged with regulation of the tribal gaming compacts. Local governments approve card rooms in their jurisdiction, as well as establish the hours of operation, table size and number, and wagering limits. The regulatory activities of these agencies are mostly funded by licensing and penalty fees collected from gaming establishments.

## **Major Provisions of the Initiative**

This measure amends the California Constitution and statutes to increase local government revenues from gambling activities. Specifically, the measure authorizes slot machines at certain California racetracks and card rooms unless all Indian tribes with existing compacts agree to specified terms.

## **Revision of Tribal-State Compacts**

In order to prevent the triggering of the measure's expansion of gambling provisions, the measure requires that all tribes with compacts agree to pay 25 percent of their "net win" to the Gaming Revenue Trust Fund (GRTF, established by the measure) and comply with certain state laws, including laws governing environmental protection, workplace, gaming regulation, and political campaign contributions. Net win is defined as the wagering revenue from all gaming machines operated by a tribe after prizes are paid out, but prior to the payment of operational expenses. A tribe

would also report its net win to the Division of Gambling Control and pay for an annual audit of its operation. All compact tribes would be required to agree to the terms of this measure within 90 days of its passage.

### **Expansion of Gambling Authorized if Compacts Are Not Revised**

The measure authorizes the expansion of gambling in the state if the tribes do not agree to the measure's new requirements. Specifically, the measure allows up to 30,000 slot machines at certain existing card rooms and horse racing tracks. The authorized facilities are located in Los Angeles, San Diego, Contra Costa, Alameda, Orange, and San Mateo Counties. The measure would allow the sale or sharing of slot machine licenses in certain circumstances. The measure also makes permanent the limit on the expansion of both the number of card rooms and the size of existing card rooms (due to expire in January 2010 under current law).

*Net Win Payments.* Owners of authorized gambling establishments would pay 30 percent of the net win from their gaming machines to the GRTF. The owners would also pay 2 percent of their net win to the city and 1 percent to the county in which the establishment is located. The measure specifies that these payments would be in lieu of any taxes or fees enacted after September 1, 2003. An owner would report its net win to the Division of Gambling Control and pay for an annual audit of its operation.

In addition to the above, affected horse racing tracks would be required to pay on an ongoing basis an additional 20 percent of the net win on their slot machines. These funds would be used to benefit the horse racing industry, including the increase of race purses.

### **Distribution of Gaming Revenues**

The measure establishes a board, comprised of five members appointed by the Governor, to administer the GRTF. The funds would be used for the following:

- Up to 1 percent of the funds for administration costs of the initiative.
- \$3 million annually for "responsible gambling" programs.
- Supplement payments to noncompact tribes to ensure that each tribe, in addition to the RSTF payments, receives a combined \$1.2 million annually.

The balance of the funds would be distributed to local governments:

- 50 percent would be provided to counties to provide services for abused and foster care children. The amount allocated to a county would be based on the county's child abuse referral reports.
- 35 percent to local governments on a per capita basis for additional sheriffs and police officers.

- 15 percent to local governments on a per capita basis for additional firefighters.

The measure also specifies that these funds could not replace funds already being used for the same purpose.

## **Fiscal Effect**

The fiscal effect of the measure on state and local governments would depend on whether compact tribes agreed to the measure's provisions within 90 days of its passage. Under either scenario, as discussed below, the measure would result in an increase in new revenues of over \$1 billion annually. As specified by the measure, these funds primarily would be provided to local governments to increase funding for firefighting, police, and child protective services.

## **Revision of the Tribal-State Compacts**

While tribes do not publicly report the net win of their gaming machines, it is estimated that the machines are generating over \$5 billion annually. If the tribes renegotiate the tribal-state compacts and agree to the measure's provisions within 90 days of its passage, tribes would pay 25 percent of their gaming machines' net win to the GRTF, over \$1 billion annually.

## **Expansion of Gambling at Card Rooms and Racetracks**

If the tribes do not agree to renegotiate the compacts within the time required, certain card rooms and horse racing tracks would be authorized to operate up to 30,000 slot machines. These entities would pay 30 percent of the net win to the GRTF. The amount of these payments would depend on the number of slot machines in operation and their net win. These revenues could potentially be over \$1 billion annually.

Also under this scenario, the cities in which these establishments are located would collectively receive payments in the high tens of millions of dollars (2 percent of the net win). Counties in which these establishments are located would collectively receive payments of half of this amount (1 percent of the net win). The use of these funds is not restricted.

*Increased Economic Activity.* If the tribes do not agree to the requirements of this measure, the measure would likely result in an expansion in gaming in the state. This would result in an overall increase in the amount of taxable economic activity in California. This would occur if, over time, there was a large diversion of gambling activity and associated spending from other states to California. This is also the case to the extent that the gaming authorized by this measure replaced existing tribal gaming activities (since much tribal activity is exempt from state taxation). This additional gambling-related activity would lead to an increase in state and local tax revenues

(property, sales, and income taxes for instance). In the longer term, the impact could be significant.

*State Regulatory Costs.* An increase in the amount of gambling in California would result in increased state gaming regulation costs. The measure provides that up to 1 percent of the GRTF may be used for these purposes.

## Summary

This measure would have the following major fiscal effect:

- Increased local government revenues of likely over \$1 billion annually from new gambling revenues. The revenues would be used primarily for additional firefighting, police, and child protective services.

Sincerely,

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Elizabeth G. Hill  
Legislative Analyst

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Donna Arduin  
Director of Finance