



Memorandum

TO: PUBLIC SAFETY, FINANCE AND STRATEGIC SUPPORT COMMITTEE **FROM:** Larry Esquivel

SUBJECT: SEE BELOW

DATE: February 5, 2015

Approved

[Handwritten signature: Jorge A. Maguire]

Date

2-12-15

SUBJECT: CARDROOM COMPLIANCE WITH TITLE 16 OF THE SAN JOSÉ MUNICIPAL CODE REPORT

RECOMMENDATION

Accept the report on cardroom compliance with Title 16 of the San José Municipal Code (Gaming Control Regulatory Program).

BACKGROUND

With the adoption of Title 16 of the San Jose Municipal Code (Code) on November 23, 1999, the Chief of Police is required to prepare an annual report evaluating the impact of cardroom gambling on crime (“annual crime report”) in the San Jose metropolitan area. On April 7, 2009, Title 16 was amended to provide the Chief of Police an opportunity to also report on regulatory issues pertaining to cardroom gambling in San Jose.

From 2009 through 2013, the annual crime report focused on the impact of cardroom gambling on crime and was presented to the Public Safety, Finance and Strategic Support (PSFSS) Committee. On April 10, 2014, as part of the annual crime report, the Police Department offered to return to the PSFSS Committee with a separate report summarizing compliance issues related to each cardroom. This report summarizes those issues.

ANALYSIS

The Regulatory Program (Title 16 of the Code)

The Division of Gaming Control (Division) is required to provide comprehensive oversight of two large gambling establishments in the City of San Jose which generate annual gaming revenue exceeding \$100 million. The City, in addition to the State, has established regulatory controls over these gambling operations to protect the public interest. The regulations include a thorough vetting process of cardroom stockowners, landowners, funding sources, and key and gambling enterprise employees; periodic audits and financial reviews to assure proper counting and recording of cardroom revenues that are subject to the City's gross receipts taxes; investigation of potential violations of Title 16 of the Code, the State Gambling Control Act and other gaming laws and regulations; and the authority to take administrative action against cardroom permittees and licensees in cases of regulatory violations to ensure future compliance.

Work Permitting

2012/2013

Most individuals working in cardrooms are required to have work permits under City and State law. In San Jose, work permits are issued by the Division. A permit fee is charged, as adopted each year by the City Council based on a cost-recovery assessment for the permitting process. During this reporting period, Garden City Inc. (currently d.b.a., "Casino Matrix") continued to experience a consistent turn-over of permitted employees. As a result, the Division processed and issued 805 work permits: 392 were new applications, 392 were renewals and the remaining were re-hires, lost badges, and name or position changes. The Division also used a *Salesforce* time-keeping system to ensure its compliance with the twenty (20) working day time-line set forth in Title 16 of the Code.

2013/2014

During this fiscal period, the Division processed and issued 446 work permits: 190 were new applications, 159 were renewals and the remaining 97 were re-hires, lost badges, and name or position changes. The Division completed this task within the twenty (20) working day time-line which is fully captured in the *Salesforce* time-keeping system.

Licensing

2012/2013

During this reporting period, Casino Matrix filed an application to amend its Cardroom Permit requesting, among other things, to relocate from its former location at 360 Saratoga Avenue (where it operated as Garden City Casino) to its current location at 1887 Matrix Boulevard. The Administrator, with the assistance of an outside consultant hired by the City, investigated and processed 3 landowner licenses. The Division also processed and issued 1 key employee license.

2013/2014

During this reporting period, the Division issued 1 stockowner renewal license; 6 regular City designated key employee licenses; 5 temporary City designated key employee licenses; 24 City temporary key employee licenses, to those holding a state interim license; and, 41 City regular key employee licenses, to those holding a state portable license. Furthermore, with the assistance of an outside consultant hired by the City, the Division investigated and processed 21 Funding Source licenses of individual applicants and 4 Funding Source licenses of business entity applicants.

Compliance Review of Cardroom Operations

In connection with the Division's review of the cardrooms' operations, administrative citations, warning letters and/or violation letters were sent to each cardroom as follows:

Casino M8trix

- October 19, 2012 – issued an administrative citation for failure to provide Division with access to the fourth floor of the tower.
- May 30, 2014 – issued a warning letter for use of un-approved gaming chips.
- July 24, 2014 – issued a violation letter for non-reporting of vendor contracts greater than \$10,000 per annum.

Bay 101

- January 7, 2014 – sent a warning for turning off of video stream to the Division surveillance system.
- July 24, 2014 – issued a violation letter for non-reporting of vendor contracts greater than \$10,000 per annum.

The Division's review of each cardroom's operations also revealed and resulted in the following:

Casino M8trix

- **Surveillance** – There was an on-going connectivity issue with Casino M8trix's remote surveillance system throughout the 2012/2013 and 2013/2014 reporting periods. Notwithstanding the active involvement of the City Manager's Office, the City IT Department and the City Attorney's Office, Casino M8trix failed to bring the system into compliance, impeding the Division's ability to observe Casino M8trix's operations through the Division's offsite remote system¹.

¹ This on-going surveillance system deficiency ultimately resulted in the City hiring an outside consultant to help address these issues which were not resolved as of the date of this report.

- **Licensing** – During the 2012/2013 reporting period, the contractor hired by the City to assist the administrator with the landowners' background investigation experienced serious difficulty obtaining necessary financial and other information from one particular applicant. The applicant refused to provide information in a timely manner, which ultimately caused the delay of the opening of the new Casino M8trix location. There is also a pending administrative action by the State of California, Bureau of Gambling Control, against Casino M8trix and two of its stockowners regarding alleged improper receipt of profits from Casino M8trix's funding source through Casino M8trix's former General Manager and the alleged use of out-of-state limited liability companies to avoid state tax liabilities and to minimize charitable contributions. This matter is on-going and the Division has cooperated with the State gaming authorities and is awaiting the State's decision regarding the stockowners' respective suitability.
- **Work Permitting** – The Division did not encounter any compliance problems associated with the issuance of work permits. 10 applications were withdrawn in 2012/2013 and 8 were withdrawn in 2013/2014 during background investigation.

Bay 101

- **Surveillance issues** – Bay 101 disconnected the streaming of video from the cardroom to the Division's remote system subsequent to the relocation of the Division offices to City Hall in October 2013. The system was re-connected within three (3) weeks after the Division addressed some security concerns.
- **Licensing** – The Division did not encounter problems with any City designated key employee background investigations during 2012/2013 or 2013/2014.
- **Work Permitting** – The Division did not encounter problems with the issuance of work permits. There were no work permit denials or revocations. 1 work permit application was withdrawn in 2012/2013 and none were withdrawn in 2013/2014 during background investigations.

Financial Review

2012/2013

With one additional Senior Auditor hired on April 28, 2013, the Division was able to begin clearing the key employee licensing backlog; conduct daily table fee collection examination, in order to monitor the proper payment of the cardroom business tax to the City; conduct several audits of cash on hand in the cardroom cages and vaults, to ensure adequate cash is maintained to redeem outstanding chips from the gambling public; and, audit cash disbursements, to ensure that payment transactions are done at arm's length. Other financial reviews included the examination of contract files, cash receipts journals, etc., to ensure that these transactions are in fact bona fide.

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2013/2014

With the addition of the Senior Auditor hired on April 28, 2013, the Division began conducting compliance reviews and audits of the cardroom finances and gaming operations. During this period, the Division examined the cardroom's available cash and cash equivalents to ensure that there is enough cash on hand to redeem all outstanding chips liabilities; reviewed vendor contracts and related disbursements, to test the legitimacy of payments; reviewed daily table fee collection information and compared to monthly tax returns, to ensure City taxes were paid correctly; and conducted potential fraud investigations relating to an independent contractor's invoices containing numbers that were different from submitted tax returns.

Staffing

The Division is currently staffed with six (6) employees consisting of one (1) Gaming Administrator, two (2) Police Officers, one (1) Supervising Auditor, one (1) Senior Auditor, and one (1) Staff Technician. Per City Council direction, the Administration is in the process of civilianizing the sworn positions within the Division and anticipates staffing those positions within the next year with trained auditors and accountants who have direct experience in the gaming industry to proactively perform inspections at both cardrooms with an emphasis on table games operation, cage and count process, and surveillance coverage to ensure gambling activities are conducted fairly and free of corrupt and criminal elements.

COORDINATION

This memo was coordinated with the City Attorney's Office and the City Manager's Office.

/s/

Larry Esquivel
Chief of Police

LE:RNT

For further questions, please contact Gaming Administrator, Richard Teng, in the Division of Gaming at (408)794-1474.