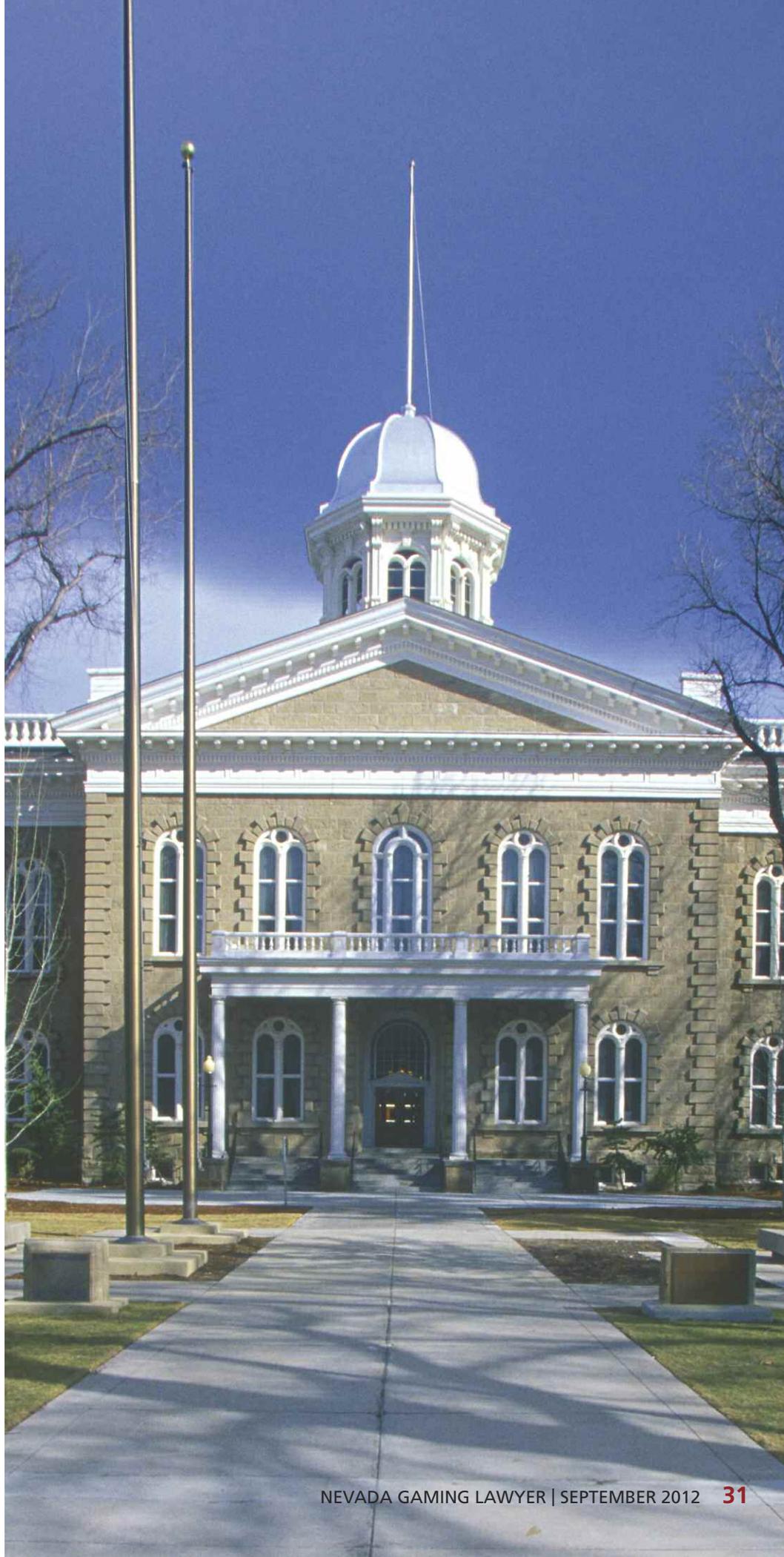


## 2013 LEGISLATIVE SESSION PREVIEW

# Crossroads for Gaming

By Matt Griffin, Russell Rowe  
and John Griffin

Commentators are often quick to state that Nevada is at a crossroads in its history. Such comments are typically spoken in the context of the state's tax structure, education policies, or a combination of both. However, this context could also be appropriately applied to the gaming industry. While the Nevada Legislature typically considers a few dozen gaming related bills during its regular session, this article will focus primarily on the broader gaming policies that the Legislature might consider when it convenes on February 4, 2013.



## Interactive (Online) Gaming

At the Gaming Law Section's 2011 Gaming Law Conference last November, Governor Brian Sandoval surprised some observers and called for Nevada's Gaming Policy Committee (GPC) to be revived, a seldom-used body that may be convened only at the call of the Governor, and only "for the exclusive purpose of discussing matters of gaming policy."<sup>1</sup>

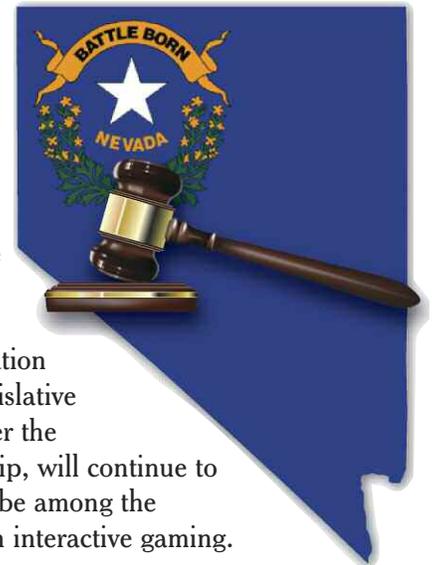
In this case, Governor Sandoval has limited the discussion of the GPC solely to issues surrounding interactive gaming, and for good reasons.

Online gaming is widely believed to be the last frontier of worldwide gaming. For Nevada, internet poker and related online gaming activities not only represents a vast, new market for Nevada's gaming companies, many of which call Nevada home for their worldwide headquarters, but is also a potentially rich environment for diversifying the state's economy into the high-technology, digital industries that support and implement interactive gaming. Nevada recognized this potential and for over a decade, the Legislature has been working with the industry to position the state to take full advantage of our industry and regulatory dominance in the gaming market.<sup>2</sup> After U.S. Department of Justice pronouncements in 2002 that use of the internet for wagering is prohibited under the Federal Wire Act, Congress adopted the Unlawful Internet Gambling Enforcement Act of 2006 (UIGEA), which effectively banned online gaming by prohibiting gaming establishments from knowingly accepting payments over the internet in connection with an unlawful wager and attacked the traditional funding sources for online gambling by making it illegal for banks and other financial institutions to collect on debt that is extended by credit cards, electronic funds transfers, checks, drafts and similar instruments.<sup>3</sup>

Undeterred, the Nevada Legislature, through guidance from the State Gaming Control Board (Board) and Nevada Gaming Commission (Commission), adopted legislation in 2011 to move Nevada closer to possibly operating interactive gaming. AB 258 authorized the Commission to develop a comprehensive regulatory structure for interactive gaming in Nevada by authorizing the licensing and operation of interactive gaming. However, AB 258 provided that a license to operate interstate interactive gaming does not become effective until: (1) the passage of federal legislation authorizing interactive gaming; or (2) the United States Department of Justice notifies the Commission or the Board that interactive gaming is permissible under federal law.

Nevada is not the only state attempting to position itself as the leader in what is already a multi-billion dollar market internationally. Illinois has adopted a similar policy and has gone one step further to become the first state to offer the purchase of its state lottery tickets online. For Nevada to meet such challenges, it must continue to study the interactive gaming market within an ever-changing technological environment and enhance its statutory and regulatory framework accordingly.

Hence, the Governor's convening of the Gaming Policy Committee. The GPC provides an environment for the thoughtful and deliberate consideration of the significant policy issues wrapped within the interactive gaming industry. These issues include, among others, preventing access to minors, blocking access from unauthorized jurisdictions, preventing hacking and protecting player data, promoting responsible gaming, preventing financial fraud and money laundering, and ensuring the integrity of virtual games. While the recommendations from the GPC are advisory only in nature, they are expected to form the basis upon which legislation will be crafted for consideration during the 2013 legislative session, which, under the Governor's leadership, will continue to position the state to be among the worldwide leaders in interactive gaming.



## Nonrestricted Gaming Policy

Considerable attention was given last year to the issue of licensing slot parlors such as Dotty's and other similar establishments. While the issue was portrayed in the media as a David v. Goliath battle between Dotty's and the larger gaming operators, the greater concern underlying the issue was the deterioration of public policies that have served as the foundation of gaming regulation in this state. With respect to Dotty's, the foundational policy at issue was the benefits Nevada enjoyed in exchange for the granting of a nonrestricted gaming license; namely, the creation of a significant number of jobs and substantial capital investment in bricks and mortar casinos and destination resorts. Putting aside the legal argument represented

by the Dotty's slot parlor model, the rapid expansion of such establishments in the state blurred the lines between restricted and nonrestricted licenses and brought into question a key policy underpinning gaming in Nevada.

The Dotty's matter was not an isolated incident in the context of the public policies guiding Nevada gaming law. The recent approval of sports kiosks outside of the traditional sports-book framework presents similar questions related to the function of restricted and nonrestricted licenses in Nevada, not to mention similar concerns related to the proliferation of casino-style wagering into Nevada's communities. As the changing gaming market continues to evolve, often at an increasingly faster pace, the traditional policies that have provided the foundation upon which Nevada's gaming industry has been built are becoming progressively more clouded.

Technology is accelerating the pace of market changes at a rate that has placed stress upon the customary statutory and regulatory governance structures. For Nevada, two (sometimes) competing but equally important broad policy objectives are in play: (1) the diversification and expansion of the gaming economy, thereby maintaining Nevada's dominance in the national and international gaming markets, and (2) the preservation of the integrity of the games and thus the sustainability of the economic model for Nevada. The GPC's focus (discussed above) on interactive gaming is an attempt by the state to get its arms around one of the driving forces behind the rapidly advancing digital gaming market and provide functional regulatory frameworks to permit the healthy growth of the market in Nevada. Whether it is online gaming or mobile gaming, or issues surrounding the evolution of non-digital gaming markets (such as slot parlors or sports kiosks), these developments require a renewed emphasis on the examination of Nevada's gaming policies to ensure that the statutory and regulatory structure allows sustainable growth while assuring that Nevada remains the gold standard in gaming regulation. These examinations will likely result in at least a few bills for consideration by the Nevada Legislature in 2013.

## **Margins Tax**

On June 6, 2012, representatives of the Nevada State Education Association and the AFL-CIO filed "The Education Initiative" with the Secretary of State's Office. The 32-page amendment to Nevada statutes employs a complicated formula to determine a business

entity's margins tax liability. In the simplest sense, a business entity's margin is the lesser of: (1) 70% of the entity's total revenue from its entire business; (2) the entity's total revenue minus the cost of goods it has sold, or (3) the entity's total revenue minus the amount of compensation it has paid its owners and employees, including employee benefits and other enumerated costs.

The Education Initiative also contains exemptions that will directly affect the application of the margins tax on casinos. Importantly, Section 25(6) of the petition allows a business entity that pays the gross gaming license fee (NRS 463.370) to exclude such revenue from the total revenue of the business. Section 29(2) of the petition also provides that gross gaming revenue shall not be used in apportioning the percentage of the business' income attributable to Nevada. The petition would not apply to businesses with total revenue that is less than \$1 million. Notably, the petition does not repeal the payroll tax, commonly referred to in Nevada as the "modified business tax" (MBT). Instead, businesses that pay the MBT (including financial institutions under NRS 363A.130) are entitled to a credit against the amount of the margins tax due from



the entity. In other words, a business that pays \$40 in MBT, and whose margin tax is \$100, will be required to pay \$100 in total taxes under this petition (\$40 in MBT, \$60 in margins tax).

At the time of the writing of this article, the petition has yet to be circulated for signatures. For the purposes of this article, we will assume that the petition will qualify for the 2014 General Election ballot, and in that case, it must first be presented for consideration by the 2013 Nevada Legislature.

Beginning from the date it convenes, the Legislature will have 40 days to enact or reject the petition.<sup>4</sup> If the Legislature rejects the petition, or if they do nothing with it, the petition will go on the general election ballot in 2014. The Legislature may also offer an alternative to the petition with the consent of the Governor. Under Article 19, Section 2 of the Nevada Constitution, any legislative alternative will appear on the 2014 general election ballot and be identified as an alternative measure to The Education Initiative.

Article 19, Section 2, thereof provides that legislation which would “conflict in substance” with the petition must be presented as an alternative to this petition on the ballot. Much of Article 19 of the Nevada Constitution has never been considered by the Nevada Supreme Court, and this section could require the Legislature to put on the ballot any reforms to the modified business tax. This might include the Governor’s proposal to extend the sunsets on certain taxes. Additionally, the Constitution prohibits amending, annulling or setting aside the terms of a petition for three years after it is approved by the voters. If the voters enact the petition, it will not take effect until January of 2015, potentially barring certain legislative amendments to the business tax structure until 2019. Again, there is little Supreme Court guidance in the interpretation of this section, but it is reasonable to assume that the disagreements over business tax legislation will spill over into the disagreements regarding the breadth of Article 19’s “conflict in substance” provision.

## Complimentary Meals

The Nevada Taxation Department is attempting to craft a regulation to implement the sales tax on complimentary meals. On February 14, 2012, the sales tax took effect; however, until the regulation is crafted and litigation settled, it appears that the Department of Taxation will accrue the tax but forego collection until these regulatory issues are resolved. Two cases on this issue, one filed by Caesars

Entertainment and one by Boyd Gaming Corporation, are currently headed to judicial review in state district court and then, most likely, onto the Nevada Supreme Court. Meanwhile, the Department of Taxation is moving forward with its rulemaking process with at least one hearing before the Nevada Tax Commission scheduled and likely more will follow. Should the Tax Commission approve the regulation, it must be heard and approved by the Legislative Commission. Given the judicial and regulatory processes, the likelihood of a regulatory or court resolution on this issue prior to the 2013 Legislative Session appears slim.



In addition to the regulatory and judicial machinations, these issues may very likely be raised before the Legislature, whether independently through a legislator’s bill draft request or as a result of budgetary forces (depending upon the possible outcomes of the judicial processes and their resultant budgetary impact). As discussed above, consideration of complimentary meals may have to take place within the context of a larger margins tax discussion, which will create a variety of policy as well as political implications that may not necessarily be tied to the merits of the complimentary meals issue.

As with most sessions of the Nevada Legislature, 2013 will be one of significant importance to the gaming industry. However, what may set 2013 apart from other sessions is that the gaming policies being discussed could be of great significance to the gaming industry and to the state not only for the near future, but for many years to come.

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<sup>1</sup> NRS 463.021.

<sup>2</sup> See Act of June 14, 2001, ch. 593, §3, 2001 Nev. Stat. 3075 (AB 466 of the 2001 Nevada Legislature, requiring that interactive gaming must be, among other conditions, capable of compliance with all applicable laws before regulations may be adopted by the Commission).

<sup>3</sup> 31 U.S.C. §§ 5361–5367.

<sup>4</sup> Nev. Const. Art. 19 section 2(3).