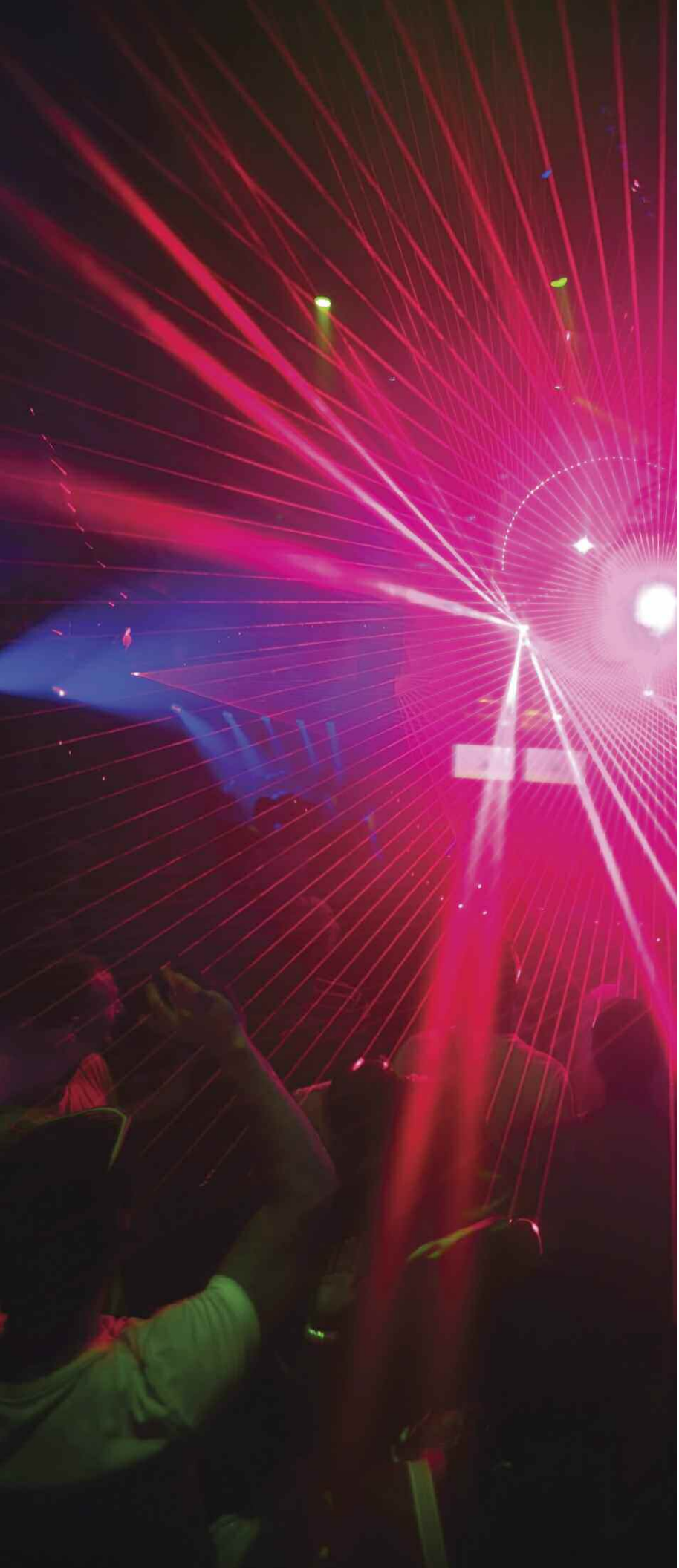

Casino Liability for Third Party Operations

By Lou Dorn

One of the more peculiar nuances of gaming law in Nevada is how certain gaming statutes and regulations have been interpreted to apply to operations that have nothing to do with gaming. You might represent an owner of a specialty restaurant, a company that operates a tattoo shop, or an operator of a nightclub, and not realize that you may have an obligation to evaluate a myriad of gaming laws, even though your client has no interest in conducting gaming operations. However, the gaming regulatory structure permeates far beyond areas typically associated with the regulation of gaming, such as the licensure of casino owners, the operation of slot machines and table games, or the collection of gaming taxes. The Nevada Legislature has declared the public policy of the State as follows:

> "Public confidence and trust can only be maintained by **strict regulation of all persons, locations, practices, associations and activities related to** the operation of licensed gaming ... and "All **establishments where gaming is conducted** and where gaming devices are operated ... must therefore be licensed, controlled and assisted to protect the public health, safety, **morals, good order and general welfare of the inhabitants of the State**, to foster the stability and success of gaming and to preserve the competitive economy and policies of free competition of the State of Nevada." (Emphasis added)[1]

This public policy exemplifies the broad sweeping nature of the many gaming statutes and regulations that impact any individual or

company with any connection whatsoever to a gaming establishment. Many people, attorneys in particular, may be left wondering how exactly a regulatory authority can regulate the "morals, good order and general welfare of the inhabitants of the State," but this is the context of the gaming minefield through which practitioners must navigate. The public policy further provides some insight as to why and how the Nevada State Gaming Control Board (the "Board") has reached beyond just the operation of the casino and scrutinized the non-gaming operations conducted within gaming establishments. While not necessarily limited to the following, those elements of a non-gaming business that may be subject to such scrutiny include its (i) security and efforts to address criminal activity, (ii) compliance with liquor and business license requirements, (iii) compliance with live entertainment taxes, and even (iv) general business, accounting and employment practices.

One reason "why" the Board is concerned with the manner in which a third party operates on the premises of a gaming establishment is that the public will generally associate the third party to be affiliated with the gaming licensee in some manner. For example, a nightclub management company whose ownership has a criminal background or conducts questionable, if not illegal, operations would reflect negatively on the owners and operators of the gaming establishment, which would tend to cause the public to lose confidence in the operation of gaming by that licensee. Another reason "why" the Board is concerned with such third party operations is the negative perception on the State and the gaming industry as a whole.

Of course, the Board's jurisdiction is limited to gaming licensees and therefore has no direct authority to regulate the conduct of non-gaming business operations. Thus, the more interesting and convoluted question is "how" the Board exerts such regulatory control. The knee-jerk reaction is that a specialty restaurant, tattoo shop or nightclub (for example) inside casinos do not conduct gaming operations in any way and therefore the Board has no jurisdiction over such operations. In fact, all this is true and the Board makes no effort to exercise any regulatory control directly over such non-gaming operations. Rather, the Board takes the position that the gaming licensee is responsible for the conduct of those third parties with operations within its property. The individual or company with a gaming license has an obvious concern here and can raise a legitimate question as to how it can be accountable for conduct which it does not control. The Board's position is that the gaming licensee should address this when it first enters into any agreements which allow third parties to operate within its premises, and include clear provisions addressing the matter in whatever transactions are used for this purpose, whether such transaction is a license, lease, management agreement or other vehicle. Accordingly, gaming companies will typically include provisions within their lease or management agreements requiring the tenant or manager to conduct (or modify) their operations in a manner that does not jeopardize the gaming company's licenses, and further require the owners and key employees of those entities to be approved by the gaming company's compliance committee.

However, what if a gaming company doesn't have such language in certain leases or management agreements, or what if a company buys a casino and inherits a long-term lease which is silent on the tenant's obligations regarding gaming compliance and regulations? This is actually quite common and puts the gaming licensee in a precarious position. The gaming licensee could find itself responding to an Order to Show Cause or a Complaint from the Board for the conduct of a tenant, and yet doesn't have the proper language in the lease agreement to either require the tenant to immediately cease certain activity or implement certain remedial measures required by the Board. The response may be to challenge the Board's regulatory authority to commence a disciplinary proceeding for the conduct of a third party. This is where the analysis of the applicable gaming statutes and regulations goes down a tortured path.

The Board will cite to a number of regulations promulgated by the Nevada Gaming Commission ("NGC"). For example, NGC Regulation 5.010(2) provides that the "[r]esponsibility for the employment and maintenance of suitable methods of operation rests with the licensee, and willful or persistent use or toleration of methods of operation deemed unsuitable will constitute grounds for license revocation or other

disciplinary action." The Board may further cite to the following acts or omissions as constituting unsuitable methods of operation:

> (8) Failure to comply with or make provision for compliance with all federal, state and local laws and regulations pertaining to the operations of a licensed gaming establishment including, without limiting the generality of the foregoing, payment of all license fees, withholding any payroll taxes, liquor and entertainment taxes and antitrust and monopoly statutes.
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> (10) Failure to conduct gaming operations in accordance with proper standards of custom, decorum and decency, or permit any type of conduct in the gaming establishment which reflects or tends to reflect on the repute of the State of Nevada and act as a detriment to the gaming industry.

The gaming licensee would naturally argue that a nightclub tenant or tattoo shop operator is not a "licensed gaming establishment" because no gaming operations are conducted within the space that they have a legal right to occupy. In fact, a typical lease agreement will include very clear language that the tenant has a leasehold interest in the applicable space and is entitled to the quiet use and enjoyment of such space without interference from the gaming landlord. Of course, if a nightclub tenant blatantly violates certain liquor laws, for example, the gaming licensee should have no trouble removing the tenant under a variety of legal theories or pursuant to other provisions in the lease. However, if the Board believes that a nightclub tenant operates with inadequate security and does not take sufficient steps to curtail criminal activities, the Board may take the position that the gaming landlord is in violation of NGC Regulation 5.010(10), yet the tenant is not violating any laws by having poor security. The gaming licensee may further counter the Board and argue that NRS 463.0148 defines an "establishment" to mean "any premises wherein or whereon any gaming is done," and since there is no gaming in the leasehold estate, the gaming regulations should not apply to the non-gaming tenant. However, the NGC defined the term "establishment" more expansively when it promulgated NGC Regulation 1.110, which defines an "establishment" to mean "any premises where business is conducted, and includes all buildings, improvements, equipment and facilities used or maintained in connection with such business." A notable jump is made from the statutory definition to the regulatory definition of the term "establishment." That jump is from the Nevada Legislature's definition of the term as any premises wherein gaming is conducted, to the NGC's definition of the term as any premises where business is conducted. Further, NGC Regulation 1.145 defines "premises" to mean "land together with all buildings, improvements and personal property located thereon." Thus, any "business" conducted on the property owned or operated by gaming licensee falls within the reach of the Board. Gaming licensees have not sought to challenge the aforementioned "long arm" of the Board, most likely due to the various provisions that make it clear that a gaming license is a revocable privilege in which the holder thereof holds no vested rights.

As referenced earlier in this article, a non-gaming tenant or operator may need to be concerned with a number of different types of activities. The most public of such activities to fall under scrutiny by the Board are the manner in which nightclubs, day clubs and similar venues address criminal activity, such as drug use, prostitution, sexual assault, over-intoxication and minors. The Board has also expressed concern as to how such operations collect fees from patrons for entry and bottle service, the handling of incapacitated individuals and restricting access to law enforcement. The Board has expressed these concerns in warning notices issued to gaming licensees and "interested parties" in 2006, 2009, and more recently in April

2012. In fact, the Board has followed up on its warning notices with formal complaints against certain gaming companies, such as the Planet Hollywood Resort & Casino in 2009 and the Hard Rock Hotel & Casino in 2010, both of which are available on the Board's website. As a result of the Board's concerted effort to eliminate unsuitable activities of this nature, gaming licensees and their nightclub tenants and operators have made significant improvements over their operations to curtail such activities.

Another area in which the Board holds gaming companies responsible for the conduct of their non-gaming tenants is the applicability of live entertainment taxes ("LET"). Any business that provides live entertainment on a gaming establishment will trigger the requirement to pay LET to the Board, irrespective if that business is conducted by the gaming licensee or by any of its tenants or third party operators. Following the same regulatory path outlined in this article, the Board will hold the gaming licensee accountable for such taxes, even if the gaming licensee was completely unaware that one of its tenants had live entertainment, and even if the gaming licensee has no access to any sales documentation necessary to determine the taxes due. For example, a specialty restaurant operating within a hotel/casino may decide to engage the services of a piano player to enhance the dining experience of its patrons. The gaming licensee is again placed in a difficult position, hoping it has the appropriate language in its lease or similar agreement with the restaurant to enable it to pass on the taxes and any resulting fees or penalties.

There doesn't appear to be any clear limitation on the Board's assertion of regulatory control over the conduct by third parties operating on a gaming establishment. For example, if a tattoo shop is found to be subject to multiple sexual harassment lawsuits, the Board could similarly deem that such an operation is contrary to the "morals, good order and general welfare of the inhabitants of this State," and seek disciplinary action against the gaming licensee (not the tattoo shop) via the same tortured regulatory path as outlined above.

As a result of the broad sweeping nature of regulatory control exercised by the Board, extreme care should be made in both the negotiation and drafting of any lease or other vehicles used to establish the relationship between a gaming company and its third party tenants and operators. If a gaming company is faced with a choice of either challenging the Board's authority on the one hand, or breaching a long-term lease on the other hand, then that gaming company has already failed to navigate through Nevada's gaming minefield.

Lou currently serves as General Counsel for the Tao Group, which operates restaurants and nightclubs in Las Vegas and New York, and recently served as General Counsel for Colony Resorts LVH Acquisitions, LLC, the owner of the LVH Hotel and Casino (formerly the Las Vegas Hilton). Lou was previously an associate with the law firm of Snell & Wilmer L.L.P. Lou is the former Chief of the Corporate Securities Division for the State Gaming Control Board in Carson City. Prior to joining the State Gaming Control Board, Lou served as a Deputy Attorney General for the State of Nevada, where he represented Nevada Gaming Commission and the State Gaming Control Board. During his five years with the Attorney General's Office, Lou also represented the Nevada Department of Transportation and the Nevada Department of Taxation. Lou received his B.A. degree from the University of Nevada, Reno in 1990, and his J.D. degree from Lewis and Clark School of Law in 1994.

[1] NRS 463.0129(1)(c) and (d).