

WRITTEN REMARKS OF MARK LIPPARELLI

CHAIRMAN, STATE GAMING CONTROL BOARD, STATE OF NEVADA

BEFORE THE HOUSE SUBCOMMITTEE ON COMMERCE, MANUFACTURING, AND TRADE

FRIDAY, NOVEMBER 18, 2011

Good morning and thank you for the invitation to provide testimony to the committee.

PERSONAL BACKGROUND

My name is Mark Lipparelli. I am the Chairman of the State Gaming Control Board in Nevada.

As you may know, Nevada is the international home of gaming entertainment in the world.

I began a professional career in 1993 managing companies whose sole focus was the design, manufacture, and sale of technology based products for the casino gaming industry around the globe. The technology includes entertainment based products, such as slot machines (which many people associate with the traditional gaming experience), but also table games and a host of systems based products geared towards making casino operations more effective, more efficient, and more secure.

In the over 18 years in the industry and the last 3 years as a member of our Board, I have personally observed a material progression in the depth and breadth of gaming technology as well as the talent and expertise that has been drawn to the industry. Early in my career, many analysts pondered cautiously how far gaming might grow beyond just Nevada and Atlantic City.

Few would have been bold enough to predict gaming's uncommon expansion now found in various forms in 48 of the 50 states with a recent opening in Queens and casino openings in Ohio next year. Gaming today is a mainstream entertainment industry across the United States, from California to Maine, and from Washington State to the Gulf Coast. Indeed, gaming is now a mainstream form of entertainment around the entire globe, and increasingly in cyberspace.

Three years ago I was asked by then Governor Gibbons to serve on the three member Gaming Control Board and I was appointed Chairman of our agency in January of this year by Governor Sandoval. The Gaming Control Board has over 50 years of proud history and its over 400 employees are responsible for the regulatory oversight of all casino gaming activities in Nevada. Areas of focus range from law enforcement activities, suitability investigations, intensive audits, the collection of taxes, employee backgrounds and registration, and, among others, the review and certification of technology exposed to the millions of customers who consume gaming in our state. My industry experience has been of great value to me in my current role but is also balanced by our statutory public policy which expresses that gaming is critical to the well-being of our state. Not only do we focus on criminal elements and ownership, but we also are increasingly concerned about the interplay of technology, innovation, and the public welfare.

GAMING REGULATORY SUCCESS

I believe it is important to provide you some perspective about the success of gaming regulation in Nevada as well as several other domestic and international jurisdictions. As you likely know, our agency was borne out of a desire by state leaders over fifty years ago to

address the infiltration of undesirables into the ownership and management of casinos in Nevada. This colorful history is well documented and intriguing, however, it does not lend sufficient credit to the many professionals who have followed from those initial focused goals. Over a long span of time, past staff and leadership in Nevada and our regulatory colleagues around the country have recognized the dynamic positive internal changes in the industry while lending support to it by substantially enhancing many areas of gaming regulation. These enhancements include robust controls over casino accounting and auditing, surveillance of gaming activities, methodologies of patron dispute resolution, world class investigative techniques, and close scrutiny and certification of technologies ranging from slot machines, electronic table games, card shuffling devices, and a wide range of integrated computer monitoring systems.

The success of regulators can and should be measured by the fact that the regulated gaming industry has been relatively free of controversy despite the industry's substantial growth and expansion. The same cannot be said of gaming markets who have not been subjected to traditional gaming regulatory rigors. As further illustration, consider in Nevada alone the amount of money wagered or "put at risk" over an average year. In our fiscal 2011, this number exceeded \$140 billion which translated to gaming revenues of approximately \$10 billion. Think about the number of hands played, the number of slot handles pulled, the number of dice rolled to equal such a number. Compare those consequential sums measured in patron activity against what are a relatively few number of patron disputes or, worse, scandal. The combination of well-developed regulation along with industry participants who

endorse strong controls has been a very successful model and given patrons the sense they are getting a fair game.

I would not represent that this success means we, as regulators, achieve perfection nor do our licensees. Our regulation, at its core, relies heavily on strong voluntary compliance and reporting by operators and imposes a range of discipline options when such compliance falls short. As a privileged license holder, our licensees realize that a reputation of careless compliance will draw undesired attention by our agents, caution letters from our leadership, the potential for monetary fines and, in the worst case, revocation of their license. This framework is established in regulatory bodies throughout the US and is important, in context. Some of the questions you wrestle with around today's topics and hard to solve only in law and will, and should, in my view, be effectively managed through the process of regulation, technical standards, compliance plans, and ultimately in disciplinary actions.

INTERNET GAMING IS HAPPENING

As the Committee considers the topic of how to approach internet poker it is critical to acknowledge that even if no progress is made towards adoption of national legislation, unregulated gaming on the internet is, and will continue to take place in many forms (many not up for Congressional consideration). The reality of Internet gambling and the public policy issues it raises appear to be something both the supporters and opponents of regulated Internet gambling agree upon. In fact, I just returned to the US from Europe yesterday following meetings with a working group of the International Olympic Committee where a broad group of experts was queried about ways to combat illegal sports wagering on the

internet and the threat such unlicensed entities pose for sports leagues around the globe. The same group cited, in its discussion, great cooperation and enhanced law enforcement techniques among those markets where internet gaming is well-regulated. Quite unfortunately, the existing dynamic in the US around internet poker continues to reward bad actors who covet US patronage while exposing risk to the very same patrons who would benefit from the protections provided by sound gaming regulation. The recent well-publicized examples of unregulated internet operators failing to protect hundreds of millions of US customer deposits can largely be attributed to an absence of the kind of regulations we regularly enforce. As our foreign regulatory counterparts become more effective in their roles as regulators (and they are) through enhanced regulation, enforcement actions and blocking of access to our citizens, US patrons who engage in online poker are more and more likely to find fewer and fewer reputable operators in our markets, further exacerbating the problem. These rogue operators have a strong profit motivation and very little, if any, motivation to create sound internal controls or enlightened policies around underage or problem gaming.

Complicating matters is the relative difficult nature of law enforcement actions, under current law, associated with entities operating unlawful internet gaming sites. Traditional methods of law enforcement such as breaking up a hidden brick and mortar back room casino are not as simple when it comes to computer networks. Often we may be able to establish the existence of an illegal gaming site but finding the wrongdoer or sponsors can be problematic. Unlike our licensees, there is no motivation to be voluntarily compliant. In many cases, these sites do violate federal law and many, unknowingly, violate specific state laws of exposing a gambling

game without a license. However, the lack of clarity, in many minds, in the federal law leads to speculation that operating an internet gaming site can be legal.

Furthermore, following years of investment in their regulatory compliance systems, licensed gaming operators and manufacturers, who have remained relatively conservative in their exposure to fast growing international internet markets find themselves at a distinct unbalanced disadvantage. One highly reputable licensee lamented to me when considering entering a market in Europe, in paraphrase, "I have played by the rules, incurred the burdens of compliance, and supported my patrons only to observe the actions of unlicensed and untaxed competitors erode my strategic position in a growing important segment of our business."

NEVADA'S EFFORT TO CRAFT REGULATION

The Committee is likely aware Nevada has recently undertaken formal steps to adopt specific regulations, technical standards, and minimum internal control systems in response to state legislation passed over ten years ago and amended in our most recent legislative session. This important work is being lead by long tenured experts in our agency and has been enhanced by legal, accounting and technical professionals who have developed decades of knowledge practicing before our agency. It has further been bolstered by the generous assistance of my regulatory colleagues in foreign markets who have, for nearly ten years, regulated internet gaming. For over two years, I have been traveling to markets outside the United States to learn and see firsthand how internet gaming is conducted, as well as the regulatory frameworks that govern these operations.

The regulations and technical standards we have created closely follow existing successful mandates of our land based operators while giving special attention to the areas particular to online poker. I am confident that our framework will be one of the more robust if not the most robust regulatory frameworks for internet gaming in existence.

It is important to note that even if we adopt our regulations and begin considering applications for formal licensure, the State of Nevada will still need to overcome legal questions associated with online poker in the absence of Congressional action. This is a requirement in our regulations and will ultimately have to be ruled on by our final licensing authority, the Nevada Gaming Commission.

I would like to strongly emphasize that Nevada's progress on these matters, in no way, minimizes or diminishes our position of support for the work you are doing today and the goal of a well constructed national piece of legislation. I, as Chairman, Governor Sandoval and many other state leaders strongly believe that Congress should act to establish a framework for state regulatory bodies to investigate and find suitable qualified applicants to conduct internet poker, establish clear regulations and standards, as well as test and certify the technology supporting internet poker. It is our preference and, we believe, the best outcome. The complexity associated with a model of legalization driven *only* at the state level will be, I believe, a missed opportunity for Congress and will not achieve the base uniformity across markets which, again, ironically will likely benefit illegal operators and handicap licensed operators. As a prime example, European markets are struggling with this topic in real time. Several EU countries who formerly allowed patrons to play cross market have established ring fenced regulated

markets of their own. Very soon after such legalization, the same countries have realized the underlying long term success of their respective markets will undoubtedly bring them squarely back to the question of cross market play and how to do that effectively while giving respect to individual country objectives. Without action by Congress, we likely will find ourselves in the same quandary.

CAN PRIMARY CONCERNS BE EFFECTIVELY MANAGED

Several questions have been raised about the ability of industry and regulators to effectively deal with the policy questions posed by internet poker including underage gaming, problem gaming, money laundering and collusion. My answer to that question is an unconditional yes.

It is abundantly clear to me that internet gaming operations have matured meaningfully in the past ten years. It is also very clear to me the underlying systems associated with internet gaming is, in nearly every case, more advanced than the types of systems (as much as they have improved) we find in our land based casinos. While land based gaming entertainment around the country can be a relatively anonymous activity, each and every patron of an internet poker site must play via from a registered account and their actions down to key strokes and mouse clicks are logged and retained. From a money launderer's perspective, this is not an attractive fact. Moreover, as licensed internet operators mature (along with their fledgling regulator counterparts), enhanced analytical tools to identify and combat issues associated with underage gaming as well as problem gaming have been developed and more will come in the very near future. In the area of problem gaming, online systems allow for various elements of self restriction (such as loss limits, access time, and self exclusion) and analytical tools are in use

to identify material changes in play levels which can be elevated to customer service representatives for analysis.

Interestingly, the gaming industry is having real impact on underlying technology trends and movement online is adding to the momentum. Years ago this would not have been so likely as moving as many people online at relatively low cost were driving internet participation. With that success in the rear view mirror, the challenges of associated with identification of account users is becoming more relevant to other industries who are in as much need to ensure they know their customer and can provide adequate levels of security. These higher demands, while not historically as relevant to wider industry, have been commonplace in gaming for years.

Interestingly, while a great deal of focus on these challenges is warranted by all of us in this analysis phase, the actual operations I have observed would indicate to me they are quite comfortable and welcome the emphasis.

Additionally, while not true across the board, many enlightened internet licensees, who operate in highly competitive markets, have developed well-constructed policy statements and training programs similar to land based operators who realize their corporate reputations are on the line with their customers. Further, many licensees who I have met have developed robust risk management functions out of their own corporate self interest.

CONCLUSION

In conclusion, I commend the work you have started and taking on this debate. It is important. Additional analysis is needed to determine the best way forward in this growing element of the

gaming industry, but I would stress that the current backdrop provides cover to those who seek undue gain at the expense of those who invest heavily in adherence of our regulatory mandates, the communities where they operate, and the patrons who are exposed.

I offer my continued assistance to you as you progress beyond today's hearing and happy to answer any questions.