Attachment A
Provided by
Reverend James Butler

CALIFORNIA COALITION AGAINST GAMBLING EXPANSION

REV. JAMES B. BUTLER, EXECUTIVE DIRECTOR

January 28, 2009

Ms. Evelyn Matteucci
Gambling Control Commission
2399 Gateway Oaks Drive, Suite 220
Sacramento, CA 95833

Re: Lucky Chances

Dear Ms. Matteucci:

I write on behalf of the California Coalition Against Gambling Expansion in opposition to renewal of the gambling license of Lucky Chances on the grounds that Rene Medina, a convicted felon, retains power to exercise influence over the gambling operation due to his familial relationship to his sons who bought the business from him, due to his beneficial interest in an Installment Note from his sons with a $42 million balance, and due to a Guaranty in his favor from the company. Neither the minimal conditions imposed on the license in September 2008, nor the transfer of the Note to a so-called "blind trust" prevent Mr. Medina's prohibited involvement in the cardroom. If this license is issued, it will establish a terrible precedent for the future, allowing cardroom owners, upon being convicted of serious violations, simply to transfer their casinos to family members, and to continue to control them behind the scenes, completely defeating the goals of the Gambling Control Act.

As you know, Rene Medina founded Lucky Chances in 1998, and he actively operated the business from 1998 to July 2007. Almost single-handedly, he grew the business to one of the largest and most successful cardrooms in the state. However, it turns out that he did not do this completely lawfully. In 2005, it was discovered that for seven years, Lucky Chances had operated with illegal betting limits, allowing many millions of dollars of illegal bets and making millions of dollars of illegal profits from them. Then, in 2006, Rene Medina was indicted by a federal grand jury for felony tax fraud. Allegations included a scheme to establish phony bank accounts in order to fake expense deductions. In 2007, Mr. Medina pled guilty to three counts of felony tax evasion.

803 VALLEJO WAY • SACRAMENTO • CA • 95818 • 916 / 441 – 1844 • CELL 916 / 420 – 8106

The Gambling Control Act was enacted "to ensure that gambling is free from criminal and corruptive elements." (Section 19801.) The Gambling Control Commission is charged with the responsibility of ensuring there is "no material involvement, directly or indirectly" by felons with the cardroom. (Section 19823.)

In August 2003, Mr. Medina first requested permission to transfer the business to his sons. The timing of this request appears to be about the time he would have learned that his 1999, 2000 and 2001 tax returns were being audited, and looks suspiciously like an attempt to circumvent the Gambling Control Act's prohibitions against licensing a felon, and to frustrate the goals of keeping gambling free of criminal elements.

On August 17, 2006, the agreement to transfer came before the Commission for approval. The Commission noted that transfer would be by sale, that the sale was for the full $48 million purchase price, that the terms of payment involved an installment note for the full $48 million, and that the interest rate would be very low. At the time, Commissioner Cruz remarked:

> I find some of the terms to be very generous.... It is an unusual transaction. It's 100% financed, very low interest rate, unsecured. I doubt very much whether if Mr. Medina were to try to sell the promissory note that he received that he would get anywhere near face value for it based on the way it's written.

The point being made is that the parties did not deal with one another at arm's length, and the lack of arm's length dealing gives rise to a presumption of control. Mr. Medina would not give these terms to a stranger. For a stranger paying over time, he would have preserved legal rights and all sorts of controls. Mr. Medina did not need to rely on legal rights here because his familial relationship with his sons. Their interests are really one.

In June 2007, just months before Mr. Medina pled guilty to these felonies; the Commission considered licensing Mr. Medina's sons, the other step in gaining approval of the transfer of the business. The Commission approved issuing a license to Mr. Medina's sons. However, recognizing Mr. Medina's continuing involvement in the business and his power to significantly influence the business, the Commission unanimously voted to impose a condition on the license that Mr. Medina remain licensed. At the meeting, Commissioner Cruz expressed two ways in which Mr. Medina's influence would continue—one financial and the other familial. Regarding the later, Commissioner Cruz remarked that Rene Medina would continue to hold a $48 million note and referred to his comments at the August 18, 2006 hearing, at which he observed that the note was for the full purchase price with low interest and unsecured.

Commissioner Cruz concluded, "so he has a vested interest in the continuing success" of the cardroom.

Commissioner Cruz was further concerned that control could be exercised through the familial relationship, the fact that the licensees were Rene Medina's sons. Commissioner Cruz said, "My concern is that I just don't know that we can police the ability or have the ability to police whether [Rene Medina] does in fact not communicate with his own sons about the operation of the club."

In October 2007, Mr. Medina entered a guilty plea, and in October 2008, he was sentenced to 15 months confinement in a federal penitentiary. As a convicted felon, Mr. Medina is not legally allowed to be involved with Lucky Chances.

Lucky Chances license came up for renewal in June 2008, and issues were raised whether Mr. Medina continues to have significant influence over the cardroom, both because of his relationship with his sons, and because of the Note he holds from his sons. The Commission continued the matter until September. In September, the Commission refused to follow staff's stringent recommendation to exclude Mr. Medina from the premises of Lucky Chances and instead merely prohibited Mr. Medina from the gaming floor. At the time, the Commission stated that conditions related to the Note would be considered subsequently.

On January 8, 2009, the Commission considered whether Mr. Medina needs to be licensed. At that hearing, Lucky Chances provided extensive testimony from three different attorneys about a proposal to transfer the $48 million Note to an irrevocable trust as a way to insulate the company from Mr. Medina's influence.

Unfortunately, the public was given no advance notice of the nature of the proposal being considered, namely, transfer of the Note to a trust, despite the fact that Lucky Chances had made the proposal to staff almost five full months earlier. The public was given notice only of an Order to Show Cause Why the Medinas Should Not Be Licensed. As a result, the public was not able to view the materials, evaluate the proposal, and make comments on it prior to that January 8 meeting. Although we still have not been allowed to review the materials submitted, such as the Note, the Guaranty, and the Trust, we take this opportunity to provide our comments now.

CALIFORNIA COALITION AGAINST
GAMBLING EXPANSION

CCAGE's attorney and lobbyist, Fred Jones, has analyzed a transcript of the Commission's January 8 meeting, and has submitted a point-by-point rebuttal of the points made at that time. A copy of that Rebuttal is enclosed. Some of the major points are as follows:

- The Medinas are the sole beneficiaries of the trust. The trustee will owe fiduciary duties to the Medinas and will be required to act in the best interest of the Medinas. This will necessarily require them to consult with the Medinas to determine the interests of the Medinas and usually, if not always, result in following the desires of the Medinas.

- The Medinas are telling two different agencies two contradictory stories. They are telling the IRS that Mr. Medina has so much interest in and control over the trust that the trust qualifies as a "grantor trust" and that transfer of the Note to the trust is therefore not taxable. However, they are telling the Commission that Mr. Medina has no right or control over the trust, and therefore he will no rights to control the Note.

- There is no testimony that the trustees are professional trustees, or even have experience as trustees. Without such experience, the trustee would be presumed to have much less independence.

- The original deal was not made at arm's length, and neither will be the trust which allows the debtors to remove and appoint new trustees, and thus choose someone who will not enforce the Note. The parties have not acted as separate parties protecting individual interests but as related parties with a single interest. Parties cannot deal with each other as having joint interests and then ask the regulators to treat them as having separate interests.

- The Medinas have not only current interests but the remainder interest. Since the Note runs for 19 more years and since the trust runs just over 2 years, the remainder interest far outweighs the current interest. The trustee will need give great weight to the Medinas desires.

- The trustee could be held personally liable for taking any action not in the best interest of the Medinas. Since the Medinas best decide what is in their interest, it would be extremely difficult for the trustee doing anything that is not approved of by the Medinas.

- There is no apparent reason for limiting the trust to a 27 month term. Since Mr. Medina retains the right to the income, the trust could be 10 years or even 20 years.

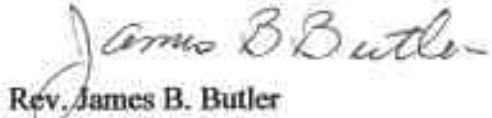
- The Guaranty by Lucky Chances in favor of Rene Medina is a direct financial obligation to him. If the sons default, Mr. Medina will get a judgment against his sons and the business, and since the only asset to satisfy the debt is the business, he will execute judgment on that and take it over. We also question whether Lucky Chances granted security for the Guaranty.

We believe that the best course of action is for the Commission to require that the sons divest their interest. At the very least, the Commission must require that the Note be refinanced by outside lenders, and that Rene Medina's financial interest in the business be terminated for good. We suggest that the Commission consider hiring an outside trust attorney to provide an independent evaluation of the proposal.

If the Commission approves this license, it will establish an awful precedent. The commission is essentially adopting a policy that once a licensee becomes convicted of a felony, even in the operation of the cardroom, the licensee can just transfer the license to family members and stay involved behind the scenes. All three Commissioners have expressed discomfort with this situation, but some have felt boxed in because of the approval given last year. However, the Commissioners cannot have it both ways. They cannot approve this license, but deny its precedential status. It will be precedent.

Thank you for considering these comments.

Sincerely,



Rev. James B. Butler
Executive Director