

FALL 2012



**NATIONAL
INDIAN
GAMING
ASSOCIATION**

REPORT

**INTERNET GAMING &
MARKETING OVERVIEW**

JE **JOSEPH EVE**
THE TRIBAL SOLUTIONS PROVIDER

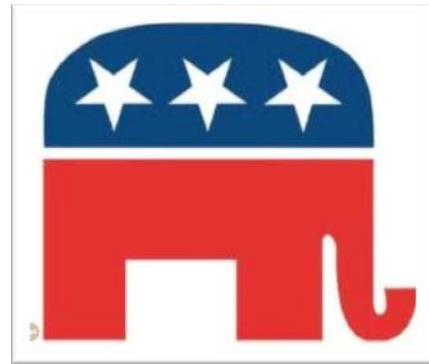


This is the Fall 2012 update to the National Indian Gaming Association's (NIGA) Internet Gaming ("iGaming") Whitepaper.

Political Update

The concern for Senator Reid's anticipated Internet Gaming bill in the lame duck session seems all but insignificant now that the Republican Party has officially stated their opposition to Internet Gaming.

"We support the prohibition of gambling over the Internet and call for reversal of the Justice Department's decision distorting the formerly accepted meaning of the Wire Act that could open the door to Internet betting," stated the GOP.



Democrats do not seem to have the will to address the subject one way or the other given what is expected to be a close presidential race. Even with Senator Kyl's support it seems clear that Reid has little if any chance of getting the votes needed to be a threat to Indian Country in the lame duck session.

The Tribal Online Gaming Act (TOGA)



In anticipation of Senator Reid's iGaming bill, the Senate Committee on Indian Affairs released its own draft bill that would allow tribes to offer internet poker. The draft was meant to generate input from Tribes in an effort to ultimately craft a federal bill that would meet the needs of Indian Country. Unfortunately, there were several contentious issues about TOGA that led many tribal leaders to disregard it.

Nevertheless, TOGA has arguably created some unanimity among tribes on the subject of Internet Gaming. Clearly there is no interest in seeing the

Secretary of Commerce or any other federal agency involved in regulating tribes on internet gaming. It is agreed that if any governing body should oversee Indian online gaming it should be the National Indian Gaming Commission.

Regarding TOGA, Tribes have expressed concerns about proposed background checks of members of a tribal governing authority, the lack of controls on



consortiums and several other issues. TOGA does give tribes the right to participate in the iGaming if Congress legalizes it and revenue generated from such business would not be subject to tax. TOGA also addresses IGRA and existing tribal state compact provisions, representing a step in the right direction.

Perhaps the most important aspect of TOGA is that tribal leaders are getting involved, discussing the issues, and determining how to deal with the complexities that iGaming presents.

Illinois Lottery Internet Gaming Lessons

The Illinois Lottery (ILL) officially launched their internet ticket sales of “Lotto” and “Mega Millions” in late March 2012 but has since seen a slow adoption rate among-would-be customers. As of August, the ILL sales were a mere \$2.2 million but the IL Lottery Superintendent, Michael Jones, remains optimistic about the future potential of the service. In a webinar in August, Jones claimed that he believed the ILL service was reaching customers that are different from their typical retail lottery customers characterized by younger age and greater (web) connectedness. Jones believes the registration process is cumbersome and believes once this is streamlined they will see a greater adoption rate. The IL Lottery has recently announced it will soon offer “Powerball” ticket sales online.



Some have speculated that the slow start to internet lottery ticket sales is attributed to the requirement of customers to submit social security information and open a IL Lottery VISA debit card as part of the account application process. The IL Lottery claims the reason for the debit card requirement is to ensure immediate payment to players on their winnings. The other reasons for requiring the Visa debit card are to facilitate credit card transactions from players and to reduce the risk associated with e-commerce transactions.



Currently a registered IL Lottery player can use their credit card to make a “deposit” into their approved IL Lottery VISA debit card account. Once this is completed the customer can then purchase electronic lottery tickets. In part, this abstraction reduces the exposure to transaction disputes or chargebacks from credit card holders.

VISA and MC member bank associations have great concern for processing Internet Gaming transactions since the implementation of UIGEA. With the introduction of “legal” internet gaming, there has been an education process in making VISA and MC



member banks feel comfortable about processing these types of credit card transactions. Large payment processors are needed to step in to assure member banks that these transactions are viable. If Tribes are one day able to offer internet gaming off-reservation, this education process will likely need to be revisited with member banks.

It is important to note that the Standard Industrial Classification (SIC) Code “7995” used by banks to identify credit card transactions for the purpose of internet gambling remains in effect.

The Illinois Lottery has already learned important lessons in iGaming e-commerce. They received complaints by customers for unauthorized charges on their credit cards for depositing into the VISA debit card account. The IL Lottery was also exposed to unnecessary risk by allowing credit card transactions from billing addresses that were different from the address listed by the customer in the registration form. Policy has now been created to require matching addresses between registration form and credit card billing to avoid exposure to fraud and transaction disputes.

Senator John Cullerton revised Illinois House Bill 4148 to authorize the Illinois Lottery to “oversee” other forms of regulated Internet gaming instead of providing these internet gaming services directly to the public. In the new version of the bill, the state could issue internet gaming licenses to current licensed gaming operators in the state (Riverboat Casinos, Race Tracks, Off-track Betting Facilities) which are termed “Affiliates”. The bill was tabled in late May but is expected to be reintroduced in the coming session. Illinois has no Indian Gaming facilities.



Senator John Cullerton (D)



Georgia Internet Lottery – Wasting No Time



The Georgia Lottery Corporation will allow players to purchase tickets for Mega Millions, Powerball and Fantasy 5. Lottery President, Margaret DeFrancisco, claims a type of game that mimics “scratch off” will be offered subsequent to the initial online lottery product offerings. Clearly Georgia is wasting little time preparing to offer a virtual gaming environment. The Georgia Lottery will also employ a similar debit card to Illinois. Georgia has no Indian Gaming facilities.

Delaware: The First State to Approve Internet Gaming

Governor Jack Markell made history when he signed legislation into law that made Delaware the first state in the union to legalize a full range of internet gaming. The law allows sports betting, casino and poker games by license gaming operators in the state. Markell hopes to launch those services in 2013 including smartphone and tablet based betting. Gaming systems will be accessible through each of the three licensed gaming operator’s websites but centrally administered by the Lottery office.



Other states in the union will be watching Delaware closely to determine how iGaming activity affects brick and mortar gaming activity and how the public reacts to these iGaming services. After the election tribes should anticipate that more states will likely push to license or operate alternative forms of internet gaming aside from the simple sale of Powerball ticket sales online. The pursuit of interactive online lottery games such as scratch-offs are the first step towards a state offered online Video Lottery Terminal (VLT) service. Delaware has no Indian Gaming facilities.



Governor Jack Markell



Internet Café Underground Betting Business Continues To Grow



Internet cafés offering video slots on computer devices in exchange for purchased internet time are flourishing all over the U.S. Many states are unclear what to do about these businesses that seem to have exploited a sweepstakes loophole in many state regulatory systems. These Internet cafés offer what amounts to real money gaming services without regulatory oversight and without gaming tax. The cost to implement such facilities is so low that at the rate that some are raided and shut down, new operations are being launched.

Many government leaders have tried to ban such establishments and others are considering regulating and taxing them. North Carolina's Governor, Bev Perdue, signed a bill making such facilities in her state illegal, but she has subsequently produced legislation that would regulate and tax these businesses to supplement the public education system, which has suffered from state budget cuts. According to the Wall Street Journal, researchers estimate gross sales from such facilities in North Carolina will exceed \$4.8 billion. "Let me be clear. I've got a record on it and I don't like sweepstakes," Perdue told reporters, but "until we can outlaw them or somehow the courts allow them to be outlawed forever, we need to tax the heck out of them and regulate them hard." Given the economic challenges states are confronted with, this type of sentiment is not uncommon among other state and county leaders. For example, the City of Marysville, Ohio has created their own legislation to legalize and tax internet cafés. Internet café's are no longer just a minor threat to Indian gaming because economic pressures are forcing state and county governments to recognize these facilities as potential cash cows for state tax coffers. Currently internet café gaming has spread to most of the United States including states like Utah where gambling is outlawed.



Tribes Partnering With iGaming Brands

United Auburn Indian Community (UAIC) became the first tribe to partner with a big Internet Gaming brand. The tribe inked a deal with Bwin.Party, the largest publically traded Internet Gaming operator in the world (based in Gibraltar). The significance of this tie up is that it is exclusive for the California market. Should Internet Gaming become legalized in California, the UAIC's Thunder Valley Casino would be the only licensed gaming operator to have well known brands like PartyPoker, PartyCasino, World Poker Tour and the expertise of one of the most successful online operators behind them.



If a version of Senator Wright's bill returns after the election, only the wealthy tribes, large commercial gaming companies and gaming consortiums in California will be able to afford the hefty state license fee (\$30m) and related start-up/operational costs. This is another indication perhaps that the formations of tribal consortiums are likely going to be a discussion topic amongst tribes going forward.

Implication of PokerStars Re-entering U.S. Market

The U.S. Department of Justice finalized a deal with Pokerstars (PS) where PS will acquire Fulltilt Poker, (FTP) making good on player balances and a civil suit to the tune of \$731 million. This will make PS/FTP yet another major iGaming settlement milestone for the U.S. Department of Justice (USDOJ).



What makes this case notable however is the fact that not only is PS/FTP expecting to re-enter the U.S. market in a big way, but the USDOJ settlement will likely prove that taking bets from U.S. residents post UIGEA was worth it for Pokerstars. Pokerstars became the biggest gaming site in the world post UIGEA and the recency of that brand leadership still resonates in the minds of U.S. players. Although Pokerstars will have paid the Fed a large sum of money for their past deeds they will be in a position to recapture the lucrative U.S. online gaming market.



Isai Sheinberg



The USDOJ will drop all civil charges against PS/FTP as part of the settlement. PokerStars founder Isai Sheinberg and a host of other PS/FTP related businessmen have been indicted for various crimes including violations of UIGEA, bank fraud, money laundering, tax evasion, etc. Some have plead guilty but there is speculation that Sheinberg will be able to pay a large sum of money to the USDOJ in a deal to avoid prosecution. This is somewhat reminiscent of the deal struck with Anurag Dikshits (founder of Party Gaming) except PS/FTP were operating well after UIGEA and in the case of FTP clearly operating without regard for ring fenced accounting.

It is not unreasonable to believe that the PS/FTP case could allow other offshore iGaming operators to come forward to confess their sins (with a fat check) in exchange for a non-prosecution agreement to gain access to the U.S. market and partner with tribes or acquire commercial casinos. Tribes should consider that other off-shore iGaming brands could make their way to U.S. soil.

Facebook and Zynga Seeking Value In Real Money Online Gaming

Recent stock valuations of Facebook and Zynga reflect the challenge both companies have meeting investor expectations, but they have more than that in common. Both companies have built a new bridge to the real money internet gaming business as a move to rescue their valuations. Facebook has introduced real money online gaming in the UK and Zynga is preparing to do something similar. Many iGaming industry professionals believe Zynga doesn't understand the regulated real money business and that they will suffer at the hands of veteran iGaming operators from Europe. Zynga and other social gaming companies believe that their ability to regularly engage millions of casual gamers puts them in an ideal position to offer real money wagering. Regardless, Facebook or Zynga will likely need to partner with or purchase licensed land-based gaming operators if they want to enter the real money gaming market in the U.S.





Social Gaming Experimentation

Despite Zynga's 16% Daily Active Users (DAU) decline on Facebook in 2nd Quarter, Facebook remains a massive pool of casual gamers.



MGM launched their Facebook social game "MyVegas" and it may be too early to determine whether this venture will be successful. The Muckleshoot tribe (WA) and Pascua Yaqui tribe (AZ) separately announced social gaming ventures recently which will give them a game presence on Facebook.

What will be most interesting to learn from these ventures is how many of these social gamers are actual casino customers and what type of casino customers they are.

The following table depicts only Facebook related games and is not an indication of popularity on mobile. These games were randomly chosen to illustrate performance differences. Daily Active Users (DAU) divided by Monthly Active Users (MAU) is a basic and common measurement of game growth trend.

Facebook Games Data		(Source: AppData)		
Game	Gamer Publisher	DAU	MAU	DAU/MAU
Chefville	Zynga	6,500,000	46,700,000	13.92%
Zynga Texas Holdem	Zynga	6,700,000	36,400,000	18.41%
Double Down Casino	Double Down Int (IGT)	1,500,000	5,200,000	28.85%
Angry Birds Friends	Rovio	1,800,000	12,800,000	14.06%
Slotomania	Playtika (Caesars)	2,100,000	6,600,000	31.82%
MyVegas	Playstudios (MGM)	40,000	320,000	12.50%

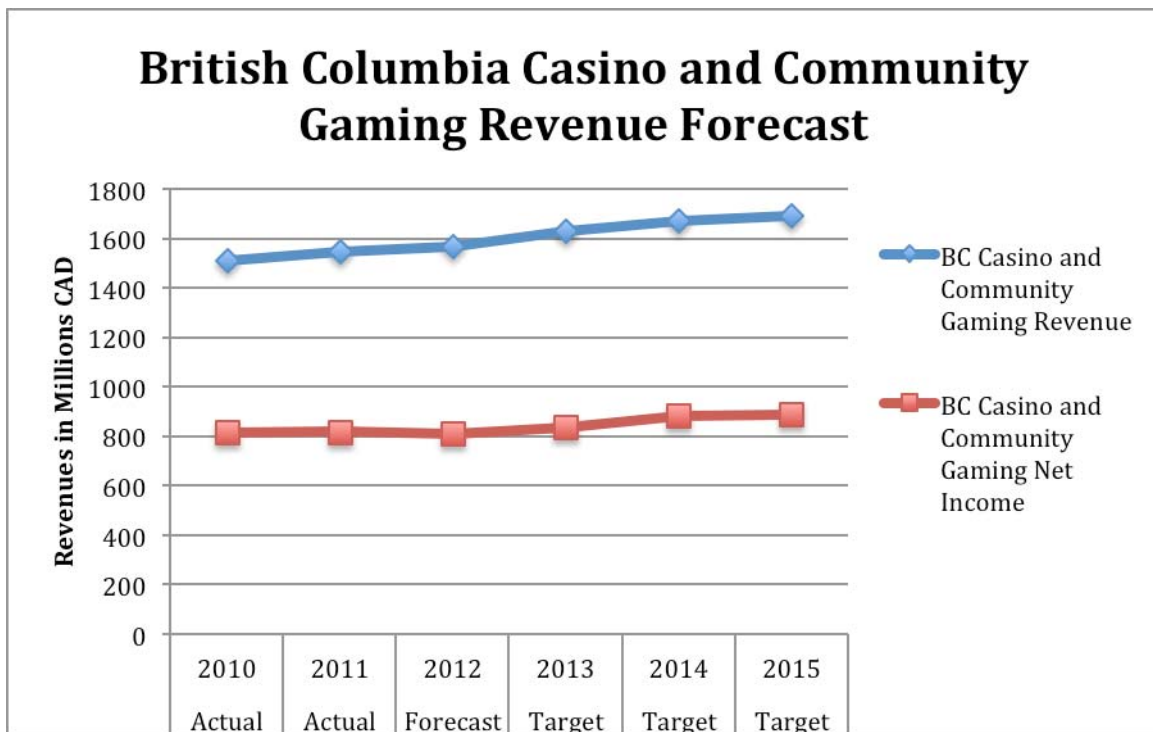
Zynga's Texas Hold'em is anomalous among most social games in that it has steadily grown over the years. Even highly popular social game titles fade over time. For example, Farmville was not long ago the most popular social game. Although Farmville is still popular today it does not rank in the top 10.



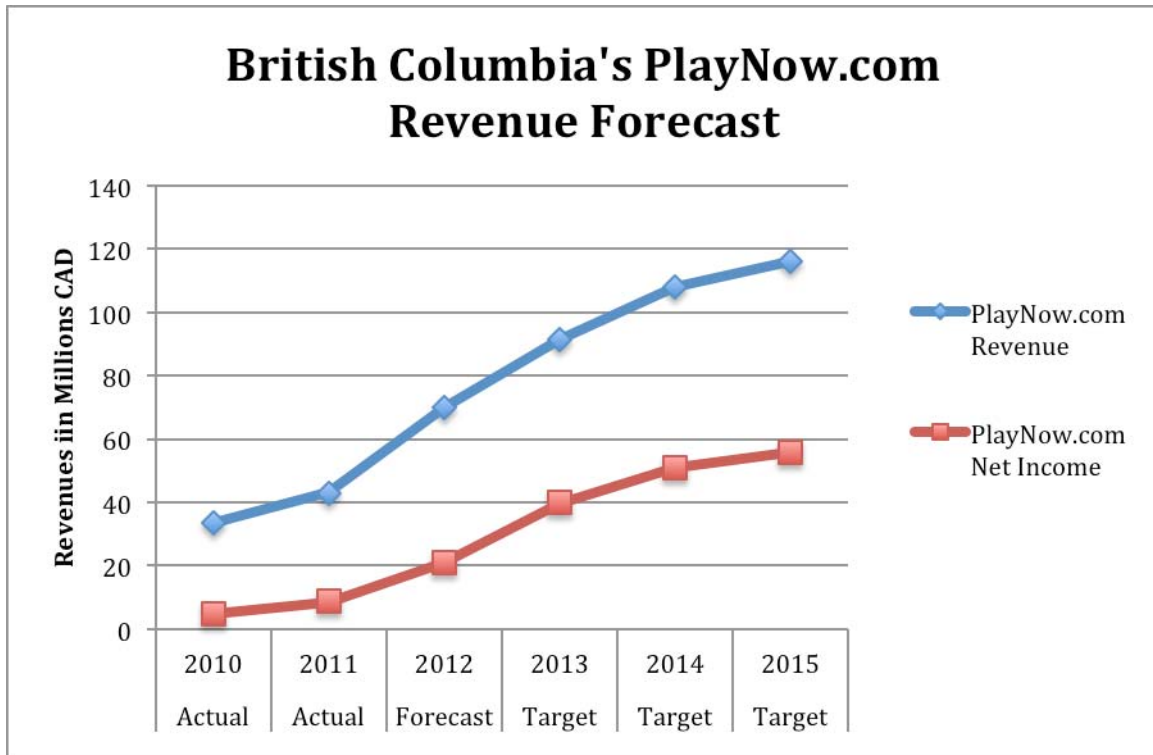
British Columbia's Casino Gaming and PlayNow.com Comparison

The following are comparisons of British Columbia's brick and mortar casino gaming revenue growth forecast and British Columbia's PlayNow.com's revenue growth forecast. BC's population is estimated at 4.57 million. BC's population over the age of 19 (19 years is legal age for gaming in BC) is estimated at 3.6 million. The province has 17 Casinos, 17 Community Gaming Centers, and 10 Bingo Halls which are independently owned but governed by the BC Lottery Corporation (BCLC).

There was 4.4% growth in BC casino revenues between 2010 and 2011 and incremental growth in casino gaming revenues is expected to continue in 2012 and beyond. Net Income in the casino sector during the same period was up \$3m to \$815.6m but is expected to be down \$8m in 2012.

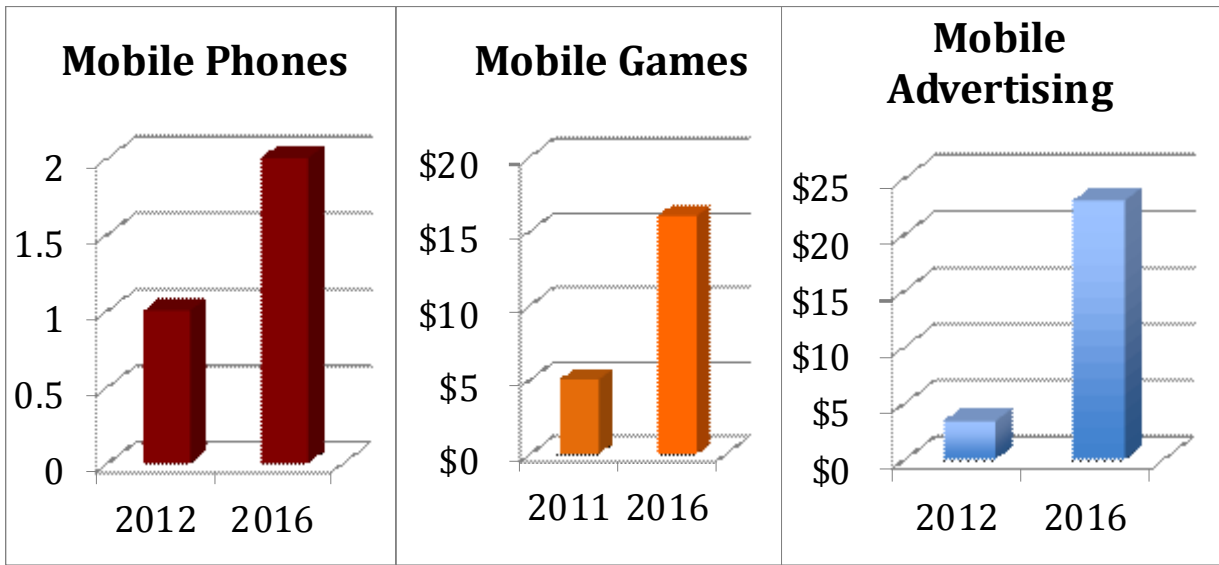


Over a three year planning period PlayNow.com net income will increase by \$36 million (136% growth). Double-digit growth is expected to increase in coming three years to 2015.



The Mobile Tsunami

There has been a dramatic surge in smartphone usage that is transforming industries including the gaming industry. ComScore estimates roughly one-third of the U.S. population is using smartphones today. Nielsen stated in March that 50.4% of all cell phone owners in the U.S. have smartphones. According to Nielsen, “games” are the most popular mobile “app” category at 64% of downloads. NPD Group, the total number of people who play mobile games grew 22% from 2011 to 2012 and the growth trend in mobile games is expected to continue. Popcap claims the average age of the mobile gamer is 39.5 years old. Zynga mobile gamers are growing three times faster than PC gamers. Facebook launched an app store called the “App Center” that will showcase mobile apps that exist on the social networking site’s platform and apps that tie in to the site using a Facebook login. Everything it seems is focusing on mobile smartphones and tablets.

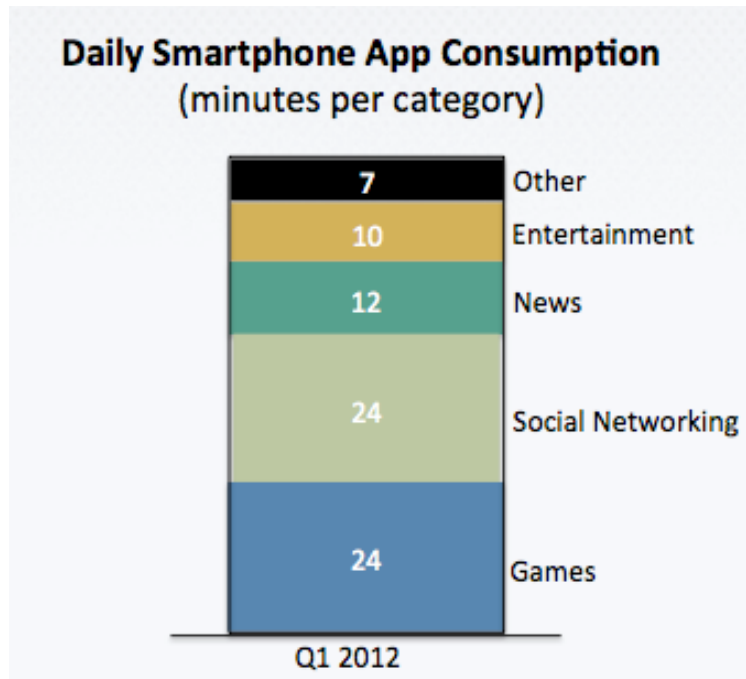


(Chart in Billions. Sources: Meeker, ABI Research, eMarketer)

Smartphone and tablet use among casino customers will have a growing effect on how tribes develop marketing strategy going forward. We know that some casinos already employ a mobile app where players can check their club points and determine what they qualify for but this is just the tip of the iceberg. There will be many breakthroughs in coming years defining new ways that tribal casinos will communicate and interact with customers while in the casino and most importantly while they are not. Tribes should be considering very seriously how to leverage mobile to instantly and efficiently drive customer behavior, as this is the new battleground of customer acquisition and retention.



The following chart shows Smartphone App Consumption by category, provided by Flurry.



Summary

iGaming presents some tough challenges ahead for Indian Country that can best be addressed through tribal leader discussions. In many states, there is disagreement among tribes over a wide range of issues, but iGaming is an issue that will likely affect all tribes so collaboration and cooperation among tribes is needed.

The economic challenges of the U.S. will likely accelerate state lottery involvement in internet based gaming regardless of who the president is in the next term. Certainly there is little will in Indian Country to open IGRA for iGaming, or tribal state gaming compacts for that matter but iGaming is not going away.

Tribes should get involved in discussions with states to determine how to best address the threat and opportunity iGaming presents. Whether iGaming has no impact, some impact or a considerable impact on brick and mortar gaming is still undetermined, but to ensure the continued growth of Indian Gaming it is prudent to perform due diligence, learn from others, discuss and develop strategy.



Mobile technologies are changing the way the world conducts business today and this transformation is happening rapidly. Tribes should be prepared to appropriate funds to these new tools and services in order to attract and perhaps more importantly retain customers. Tribes can consider this not only as an investment in their existing business, but a way to be prepared for the prospects of regulated iGaming.

JOSEPH EVE

JOSEPH EVE (JE) is a CPA & Consulting firm that specializes in Indian Country providing cloud computing technologies, casino audits, outsourced accounting services, NIGC MICS compliance reviews, internal audits, contract controller services, custom and National seminars, internet gaming consulting, business planning, and consulting services throughout the United States. In addition, we facilitate seminars throughout each year on casino related topics. JE has been serving tribal governments, tribal casinos and tribal entities since 1983.

JE currently serves clients from Washington DC to San Diego. A few current and past gaming clients include Ho-Chunk Gaming, Osage Million Dollar Elm Casinos, Sycuan Casino and Resort, National Indian Gaming Association (NIGA), and Harrah's Rincon Casino.

JE publishes the annual Cost of Doing Business report (CODB) that compiles information from over 85 casinos with the results used by many casinos as a business management aid to help analyze many unique financial metrics specific to tribal gaming.

Disclaimer

JOSEPH EVE is not responsible for projections in this overview report. These projections are based on research and assumptions by JOSEPH EVE and industry specialists. As Internet gaming is operated globally and highly unregulated in many areas, it is impossible to retain exact financial figures. We have made our best effort to provide reliable, accurate, and reasonable information.

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Questions/Comments

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Ehren Richardson – iGaming Consultant

Ehren introduced the first browser-based casino and poker software (written entirely in Java) in the 90's that helped grow Internet Gaming brands like "BODOG". Ehren later led a design and production team contracted to Electronic Arts Black Box to produce versions of "Need For Speed", the most successful racing game franchise of all time. With SEGA Ehren co-developed the "Royal Derby" video horse racing game acquired by Shuffle Master. He has also been involved in various award winning adver-game initiatives including the "Fashionista Challenge" and the "Degree Poker Championship" with brand sponsors such as Unilever, TSN, ESPN, MSN-Bell Canada.

Ehren is an indigenous Hawaiian (Kānaka Maoli) and registered member of The Office Of Hawaiian Affairs (OHA). He is involved in the Hawaiian sovereignty movement and supports the Hawaiian Governance Initiative (Hoꞑoulu Lāhui Aloha).

Grant Eve CPA, CFE

Grant is a Partner at JOSEPH EVE. He brings several years of industry experience with and was previously employed at Deloitte LLP in Las Vegas, Nevada, in the firm's National Gaming Practice. Mr. Eve has been closely following internet gaming and recently testified before the US Senate Committee on Indian Affairs oversight hearing "Internet Gaming; What's at Stake for Tribes." He has also spent time in Washington DC visiting with multiple congressmen and senators, and the National Indian Gaming Association. He has provided Internet gaming consulting services for NIGA and presented on Internet gaming at the following tradeshow: Washington Indian Gaming Association Annual Tradeshow, Sycuan Casino & Resort Seminar, Oklahoma Indian Gaming Association Annual Tradeshow, National Indian Gaming Association Mid Year Meeting, National Indian Gaming Association Tribal Leaders Membership Meeting, National Indian Gaming Association Internet Subcommittee, and the National Indian Gaming Association Annual Tradeshow.

