

COMMONWEALTH OF PENNSYLVANIA

GAMING CONTROL BOARD

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PUBLIC HEARING

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BEFORE: DAVID M. BARASCH, CHAIRMAN
Gregory C. Fajt; Richard G. Jewell; Keith
R. McCall; Anthony C. Moscato; William H.
Ryan, Jr.; David W. Woods; Members
Fred Strathmeyer, Jr., representing Russell
Redding, Secretary of Agriculture
Jennifer Langan, representing Timothy
Reese, State Treasurer
Robert P. Coyne, representing Eileen H.
McNulty, Secretary of Revenue
HEARING: Wednesday, February 10, 2016, 10:01 a.m.
LOCATION: Bureau of Hearings and Appeals
Strawberry Square Complex
Suite 261
Harrisburg, PA 17106
WITNESSES: Brian DiMattia, Frank Quigley

Reporter: Samantha Bruer

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A P P E A R A N C E S

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A P P E A R A N C E S (Cont.)

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ORAL ARGUMENT

By Attorney Sklar

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ORAL ARGUMENT

By Attorney Tepper

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DISCUSSION AMONG PARTIES

17 - 25

E X H I B I T S

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NONE OFFERED

P R O C E E D I N G S

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CHAIRMAN:

Let's move on to the next argument,
please. Thank you very much.

ATTORNEY STEWART:

Thank you, Chairman. Thank you,
Commissioners.

CHAIRMAN:

Good morning. Would both Counsel please
identify themselves and spell their names for the
court reporter?

ATTORNEY TEPPER:

Good morning, Chairman Barasch, members
of the Board. David Tepper, T-E-P-P-E-R, with the
OEC.

ATTORNEY SKLAR:

Good morning, Mr. Chairman and members
of the Board. Michael Sklar, S-K-L-A-R, on behalf of
Mount Airy Number One, LLC.

CHAIRMAN:

And you may begin.

ATTORNEY SKLAR:

Thank you. The request that's before
you is to revise Mount Airy's Audit Committee charter

1 to permit one owner to serve on the Audit Committee.
2 Currently, the charter prohibits an owner from serving
3 on the Audit Committee, and I'm going to be brief,
4 because I'm sure you've read the materials that have
5 been submitted, the briefs. The purpose of an Audit
6 Committee is twofold. Number one, it's to assist a
7 Board of Directors in the oversight of a company.

8 And number two, it's to protect the
9 shareholders of the company. Sarbanes-Oxley was
10 passed, as everyone knows, in the wake of accounting
11 scandals at Enron and WorldCom. And in the preamble
12 to Sarbanes, it specifically says the purpose of the
13 Act is to protect investors. In addition, the
14 American Institute of Certified Accountants publishes
15 an Audit Committee tool kit for private companies, and
16 both Enforcement Counsel and Mount Airy have cited to
17 that publication.

18 And in that publication, it also
19 reinforces what's in Sarbanes, that the Audit
20 Committee represents the interests of all owners of
21 the business. At Mount Airy, the shareholders are the
22 owners of the company. It's an LLC, so we don't have
23 shareholders. But we have members, and they're the
24 owners of the company. All of the members of Mount
25 Airy are members of the DeNaples family.

1 The Board of Directors at Mount Airy is
2 called the Management Committee. It's kind of a
3 misnomer. Again, it goes back to the fact that Mount
4 Airy is formed as a Limited Liability Company.
5 There's managers, so it's called a Management
6 Committee. But essentially, it functions as a Board
7 of Directors. Mount Airy's Audit Committee currently
8 is comprised of two members that are completely
9 independent of Mount Airy and the DeNaples family.

10 The Chairman is Lance Cole. He's a
11 professor at Dickinson School of Law, and he's a
12 Director of Dickinson's Center for Government Law and
13 Public Policy. The second member is Pat Ross. He was
14 formerly a teacher for 23 years and supervisor of
15 Pocono Township for 20 years, and he currently runs a
16 consulting company that assists businesses in business
17 development. Unfortunately, the third member passed
18 away.

19 He was a CPA, a former employee of the
20 IRS, and that's what precipitated the current request
21 to fill that spot. And the --- what's contemplated
22 right now is to add Dr. Louis DeNaples, Jr. as a
23 member of the Audit Committee. He's highly qualified.
24 He is currently a licensed Principal before the Board.
25 He is a licensed medical doctor. He's the owner of

1 several medical businesses.

2 He currently serves as a Vice Chairman
3 of a publicly traded company. Also serves on the
4 Audit Committee, Risk Management Committee and
5 Corporate Governance Committees of that publicly
6 traded company. He's also a shareholder of that
7 company. The request is not breaking new ground here.
8 The Board has permitted and continues to permit
9 another privately held Licensee to have one of its
10 owners serve on that company's Audit Committee.

11 The Enforcement Counsel's arguments just
12 don't really ---. It doesn't make much sense, the
13 arguments they're making. The first argument they
14 make is the Audit Committee must be independent of the
15 Board of Directors. That's directly contrary to both
16 Sarbanes and the American Institute of Certified
17 Public Accountants' publication, because they
18 specifically contemplate that it is the members of the
19 Board of Directors that are going to serve on the
20 Audit Committee.

21 Secondly, they say having an owner serve
22 on an Audit Committee would compromise the Audit
23 Committee and make its work product suspect. Again,
24 there's precedent for this, and the fact that another
25 Licensee is currently doing it, I think, belies the

1 argument that OEC is making. And lastly, OEC contends
2 that it's contrary to the existing charter to allow
3 this to happen.

4 Well, that's the whole purpose why we're
5 here. We understand that it's currently prohibited,
6 and any amendments to the charter require Board
7 approval. And that's the precise reason why we're
8 coming before you with this request. That's all I
9 have, and I'm happy to answer any questions.

10 CHAIRMAN:

11 Thank you. OEC, your response?

12 ATTORNEY TEPPER:

13 Good morning, Chairman Barasch and
14 members of the Board. As Mr. Sklar said, Mount Airy
15 is requesting that the Board permit one of their
16 owners, Dr. DeNaples, to serve on their Audit
17 Committee. I'm briefly going to highlight some of the
18 reasons that OEC objects to this request, including
19 that it's contrary to the Board's regulations. Having
20 a non-independent member of the Committee could create
21 a conflict in the reporting structure for the
22 Surveillance, Audit and Compliance Departments.

23 In their statement of conditions, the
24 Board approved charter and the Board's regulations all
25 require them to have an independent Audit Committee,

1 and this would be falling in line with the spirit of
2 the best practices set forth by the American Institute
3 of Certified Public Accountants, or the AICPA. Doctor
4 --- I'm just going to start off with the premise. Dr.
5 DeNaples is not an independent individual.

6 He is one of three DeNaples family
7 members that serves on the Management Committee, which
8 fulfills the role of the Board of Directors at Mount
9 Airy. But he also serves as one of those three same
10 family members that is a trustee on the trusts that
11 own Mount Airy's holding company, which owns 100
12 percent of Mount Airy Number One, LLC. He is at a 50
13 percent ownership interest in one of those seven
14 trusts, and he is a family member of every other Mount
15 Airy Principal save the two covered Audit Committee
16 members.

17 As the Board regulations require that
18 the Directors of Mount Airy's internal audit and
19 surveillance departments report to an independent
20 Audit Committee or other designee regarding there is a
21 policy, purpose, responsibility and authority.

22 Pursuant to the Board's authority in
23 Section 465A.11(c)(5), the Board, through Mount Airy's
24 signed statement of conditions, has designated that
25 the Directors of Internal Audit, Compliance and

1 Surveillance report to the Audit Committee regarding
2 members of policy, purpose and responsibility and
3 authority.

4 Further, pursuant to this Board
5 regulation, the hiring, firing and the salary of these
6 three important Directors is set by an independent
7 Audit Committee and not the Management Committee.
8 This regulation is in place so that these supervisors
9 of Surveillance, Independent Audit and Compliance have
10 an ability to discuss internal matters and raise
11 concerns. But they could be reluctant to do so if
12 Management Executives are members of the Committee.

13 And having them report to an independent
14 Audit Committee is significant for the policy,
15 purposes and responsibility. And having that
16 independent Audit Committee responsible for hiring,
17 firing and salary while the Management Committee
18 directs their day to day operations ensures
19 independence and prohibits a potential conflict of
20 interest from occurring.

21 Similar to the three department heads
22 who I've just talked about, the other two members of
23 the Audit Committee may be hesitant to speak out or
24 voice concerns at a closed meeting if they know that
25 an owner is present who controls their own contracts

1 being renewed. Mount Airy's current Audit Committee
2 charter has multiple controls and clauses which ensure
3 that there's no material relationship between an Audit
4 Committee member and Mount Airy or of any one of its
5 Principals.

6 And having Dr. DeNaples serve on this
7 Committee would eviscerate all of those clauses that
8 the Board and Mount Airy has put in place to ensure
9 independence.

10 Further, Mount Airy has offered and
11 agreed since its inception to have an independent
12 Audit Committee. During Mount Airy's initial
13 suitability hearing, through their attorney, they
14 offered that --- to the Board that if granted a Slot
15 Machine License, they would form an independent Audit
16 Committee which would have the absolute authority and
17 responsibility to monitor and report on the operations
18 and financial controls of the company.

19 As the Board knows, Mount Airy was
20 granted a Slot Machine License by the Board in
21 December of 2006. It signed its first statement of
22 conditions in April, 2007, where they agreed to have
23 an independent Audit Committee. Mount Airy's initial
24 independent Audit Committee charter was filed with the
25 Board in October 2007 and required that the Audit

1 Committee members be independent.

2 It also listed five financial
3 relationships which would constitute an individual
4 having a material relationship with Mount Airy and
5 that would then disqualify the individuals from
6 serving on Mount Airy's independent Board of
7 Directors. Mount Airy signed a statement of
8 conditions with the Board again in December --- or
9 sorry, in February of 2010 and in September 2012,
10 where they agreed to maintain an independent Audit
11 Committee.

12 In June 2012, the Board issued an Order
13 approving a new charter for Mount Airy's Audit
14 Committee, and that charter also continued to place
15 restrictions on who can serve on the Audit Committee
16 and including prohibited Principals and others who
17 have a material relationship from serving on the Audit
18 Committee. This was done to keep the Audit Committee
19 independent for the reasons that we've both talked
20 about prior.

21 And that's listed in our brief, and that
22 is the charter that we are operating under today. It
23 is contrary to the best practices. The AICPA says
24 that, in the Sarbanes-Oxley requirement, that each
25 member of the Audit Committee shall be a member of the

1 Board of Directors and shall be independent as a best
2 practice. Unlike the privately --- or publicly traded
3 companies, Sarbanes-Oxley does not apply to them.

4 It's not law. Mount Airy cannot fully
5 meet this best practice because it doesn't have any
6 independent directors serving on its Management
7 Committee, unlike a traditional company. It doesn't,
8 also, have a Board of Directors. However, the policy
9 of having an independent Audit Committee can still
10 work here. The Audit Committee being independent is
11 significant, because it has an important corporate
12 oversight function, insofar as it provides oversight
13 to the company's finances, audit, legal and regulatory
14 requirements.

15 And these may contradict an owner's
16 wishes. Mount Airy argues that they're being cheated
17 because at least one other privately owned casino has
18 an owner on its Audit Committee. However, unlike
19 every other Licensee, Mount Airy is the only casino
20 wholly owned by family members. Other Slot Machine
21 Licensees are owned by individuals or entities that
22 operate at arms' length business agreements with each
23 other. And each individual in those operates for
24 their own economic interests in an arms' length
25 transaction with each other. However, Mount Airy's

1 operated by family members who might make sacrifices
2 for each other and who further might be motivated by
3 --- not by profit, but by mutual admiration and mutual
4 affection.

5 In conclusion, the regulations require
6 that the Directors of Internal Audit and Surveillance
7 report to an independent Audit Committee on members of
8 policy, purpose, responsibility and authority and to a
9 Management Committee on administrative and daily
10 matters. This ensures that there's independence and
11 there's a reduction of a conflict of interests. The
12 Directors of Internal Audit, Surveillance and
13 Compliance Departments can be reluctant to discuss
14 internal matters or raise concerns when they know an
15 owner is present. Mount Airy has agreed to have an
16 Audit Committee. They offered to have one, and OEC
17 today asks that they be held to this requirement.
18 Thank you, and we'd be ---

19 CHAIRMAN:

20 Thank you.

21 ATTORNEY TEPPER:

22 --- able to answer questions.

23 CHAIRMAN:

24 Thank you. Are there any questions from
25 the Board? All right.

1 MR. FAJT:

2 Thank you, Mr. Chairman. Mr. Sklar, is
3 the Audit Committee paid?

4 ATTORNEY SKLAR:

5 Yes, the --- \$40,000 a year. If the
6 Board grants the Petition, Dr. DeNaples is appointed,
7 he will not be paid.

8 MR. FAJT:

9 Okay. Mr. Tepper, what about Mr.
10 Sklar's argument that this Board does allow another
11 individual who is an owner of a casino, partial owner,
12 to serve on its Audit Committee?

13 ATTORNEY TEPPER:

14 I think that that --- we take ---. OEC
15 and the Board takes every instance and every
16 application on its own, and we're here talking about
17 Mount Airy, which is solely owned by one family rather
18 than a corporation that has people at arms' length
19 transactions. The ownership interests of the
20 individuals are completely different.

21 MR. FAJT:

22 And lastly, Mr. Sklar, what are your
23 thoughts or what's your argument about Mr. Tepper's
24 statement that a Board Order, I believe you said, was
25 dated June 12th limiting who can serve on the Audit

1 Committee and specifically barring somebody with a
2 financial interest in the casino from serving on that
3 Audit Committee?

4 ATTORNEY SKLAR:

5 The June 12th --- I mean, the
6 requirement about the Audit Committee dates back ---.
7 It's not June 2012. It dates back to the beginning of
8 when Mount Airy was licensed. So, there's no ---.

9 MR. FAJT:

10 But there was an amendment. I thought
11 that you had said that there was the latest amendment
12 to this Board Order, or something you specified was
13 --- I thought you said ---

14 ATTORNEY TEPPER:

15 Yes. There is a ---.

16 MR. FAJT:

17 --- that was a June 12th or June 2012?

18 ATTORNEY TEPPER:

19 June 2012. There was a --- the Board
20 issued an Order approving a new charter, and Mount
21 Airy redid their Audit Committee charter around that
22 time. And there were several Board Orders, the last
23 one being June '12 ---

24 MR. FAJT:

25 Okay.

1 ATTORNEY TEPPER:

2 --- June of 2012.

3 MR. FAJT:

4 And in that Board Order, did you not
5 state that we limited who could serve on that Audit
6 Committee?

7 ATTORNEY TEPPER:

8 Yes, I believe the Board Order states
9 that it must comply with the charter. The charter
10 limits who can serve on the Committee.

11 MR. FAJT:

12 And one of the bars to who can serve on
13 the Committee is that somebody with a financial
14 interest in the casino cannot serve on that Committee?

15 ATTORNEY TEPPER:

16 Yes.

17 MR. FAJT:

18 All right.

19 ATTORNEY SKLAR:

20 My point was that that wasn't a new
21 restriction in June of 2012. That was a restriction
22 from 2007.

23 MR. FAJT:

24 Okay.

25 ATTORNEY SKLAR:

1 That's where --- the genesis of it.
2 Again, the way this came up was the passing of one of
3 the Audit Committee members. The Management Committee
4 just had a meeting. They discussed, you know, who
5 would fill the vacant spot, and they called me and
6 said, can Dr. DeNaples serve? And I said to them, the
7 Audit Committee charter right now prohibits it. If
8 that's the direction you want to go in, we're going to
9 have to file a petition and make our case before the
10 Board. And that's the sequence here.

11 MR. FAJT:

12 Okay.

13 ATTORNEY SKLAR:

14 And can I just make two comments in
15 response to ---? I promise I'll be brief.

16 CHAIRMAN:

17 You need to be brief.

18 MR. FAJT:

19 Uh-huh (yes).

20 ATTORNEY SKLAR:

21 I will. The independence requirement
22 for Audit Committees is independent from day to day
23 management. That's the independence that's required.
24 So, here, Dr. DeNaples is independent from the day to
25 day management. Lisa DeNaples is the owner and

1 managing trustee. She does not run the day to day
2 operations. That's vested in the General Manager,
3 John Culetsu.

4 The regulation that Mr. Tepper cited, in
5 terms of the direct reports ---. He did not include,
6 it's more expansive than just the direct --- that
7 those three department heads have to report to an
8 independent Audit Committee. That's one of the bodies
9 it can report to. It could also report to a Board of
10 Directors. There is no requirement anywhere in the
11 Gaming Act or the Board's regulations that casinos
12 have to have an Audit Committee.

13 You know, there was a proposed
14 regulation, as some of you may be aware, back in 2008,
15 and it was never adopted. So, there is no requirement
16 in Pennsylvania under the Pennsylvania gaming laws
17 that requires casinos to have an independent Audit
18 Committee.

19 CHAIRMAN:

20 Thank you. Any other questions from the
21 Board?

22 MR. MOSCATO:

23 Thank you, Mr. Chairman. Mr. Tepper, I
24 appreciate the fact that you or that OEC looks at each
25 case individually and on its own merit. But would it

1 be fair to say that with the other casino that has an
2 owner on the Audit Committee, that that casino is also
3 more or less controlled by a family?

4 ATTORNEY DAVENPORT:

5 In this case, no. There are other
6 individuals or entities that ---. It's not one family
7 that would control the facility, so I think it can be
8 distinguished in this case.

9 MR. MOSCATO:

10 They are minor shareholders.

11 ATTORNEY DAVENPORT:

12 Yes, but in this case, Dr. DeNaples is
13 family members of all --- and a trustee of all the
14 other trusts for the 100 percent owner Holdco of Mount
15 Airy Casino.

16 MR. MOSCATO:

17 But the individual on the Audit
18 Committee is employed by the casino also?

19 ATTORNEY DAVENPORT:

20 We'd have to look into that. I'm sorry.
21 I don't --- I'm sorry?

22 ATTORNEY PITRE:

23 You're referring to the other casino?

24 MR. MOSCATO:

25 Yes.

1 ATTORNEY PITRE:

2 That individual is not employed by the
3 casino. He is part of the Management Committee of the
4 casino or the Management Company of the casino.

5 MR. MOSCATO:

6 So, he's employed by the Management
7 Company ---

8 ATTORNEY PITRE:

9 Right, of ---.

10 MR. MOSCATO:

11 -- of the casino?

12 ATTORNEY PITRE:

13 And he is not a family member of any
14 other individual that owns the casino.

15 MR. MOSCATO:

16 Thank you.

17 CHAIRMAN:

18 Any other questions?

19 MR. WOODS:

20 If I --- perhaps this has already been
21 stated, but just to make it clear. As I understand
22 it, this other casino isn't required by the Board to
23 have an Audit Committee; isn't that correct?

24 ATTORNEY PITRE:

25 The Board does not require any casino

1 other than this casino to have an Audit Committee.

2 MR. WOODS:

3 Okay.

4 ATTORNEY PITRE:

5 All of the other casinos have an Audit
6 Committee.

7 MR. WOODS:

8 Okay.

9 CHAIRMAN:

10 We're going to take a ten-minute recess.

11 Thank you.

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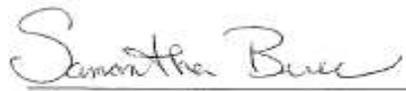
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CERTIFICATE

1
 2 I hereby certify that the foregoing
 3 proceedings, hearing held before Chairman Barasch was
 4 reported by me on 2/10/16 and that I, Samantha Bruer,
 5 read this transcript, and that I attest that this
 6 transcript is a true and accurate record of the
 7 proceeding.

8 
 9 Court Reporter
 10 Samantha Bruer

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