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**COMMONWEALTH OF KENTUCKY**
**SUPREME COURT OF KENTUCKY**
**CASE NO. 2012-SC-000416-D**

**KENTUCKY HORSE RACING COMMISSION, APPELLANT,**

**vs.**

**ON APPEAL FROM THE KENTUCKY COURT OF APPEALS**
**CASE NO. 2011-CA-00164**
**(FROM THE FRANKLIN CIRCUIT COURT)**
**(CASE NO. 2010-CI-1154)**

**THE FAMILY TRUST FOUNDATION**
**OF KENTUCKY, INC.,**
**d/b/a THE FAMILY FOUNDATION, APPELLEE.**

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**BRIEF OF THE APPELLEE,**
**THE FAMILY TRUST FOUNDATION**
**OF KENTUCKY, INC., d/b/a**
**THE FAMILY FOUNDATION**

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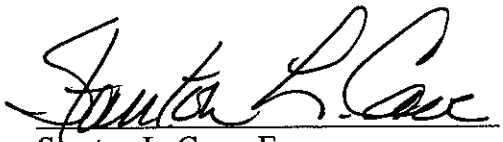
## CERTIFICATE OF SERVICE

I do hereby certify that a copy of the Brief of the Appellee, The Family Trust Foundation of Kentucky, Inc., d/b/a The Family Foundation, was served by depositing same in the United States Mail, first class, postage prepaid, address to the following: Laura M. Ferguson, Esq., Douglas M. Dowell, Esq., Office of Legal Services for Revenue, P.O. Box 423, Frankfort, KY 40602-0432; Jeff Mosley, Esq., Finance and Administration Cabinet, 702 Capitol Avenue, Frankfort, KY 40601; Peter F. Ervin, Esq., La Tasha Buckner, Esq., Office of Legal Services, Public Protection Cabinet, 500 Mero Street, 5th Floor, Frankfort, KY 40601; Susan B. Speckert, Esq., Kentucky Horse Racing Commission, 4063 Ironworks Parkway, Bldg. B, Lexington, KY 40514; William A. Hoskins, Esq., Jay E. Ingle, Esq., Jackson & Kelly, PLLC, 175 East Main Street, Suite 500, Lexington, KY 40507; William M. Lear, Jr., Esq., Shannon Bishop Arvin, Esq., Christopher L. Thacker, Esq., Stoll Keenon Ogden PLLC, 300 West Vine Street, Suite 2100, Lexington, KY 40507-1801; Sheryl G. Snyder, Esq., Jason Renzelmann, Esq., Frost Brown Todd LLC, 400 West Market Street, 32nd Floor, Louisville, KY 40202; Samuel P. Givens, Jr., Esq., Clerk of the Court of Appeals, 360 Democrat Drive, Frankfort, KY 40601; The Honorable Thomas Wingate, Judge, Franklin Circuit Court, 669 Chamberlin Avenue, Frankfort, KY 40601, on this the 10th day of May, 2013.

I do hereby further certify that the record was not removed by me from the Franklin Circuit Court or the Kentucky Court of Appeals.



Stanton L. Cave, Esq.
LAW OFFICE OF STAN CAVE
P.O. Box 910457
Lexington, KY 40591-0457
Telephone: (859) 309-3000
Facsimile: (859) 309-3001
Email: stan.cave@insightbb.com
*Counsel for the Appellee, The Family Trust Foundation of Kentucky, Inc., d/b/a The Family Foundation*

## I. INTRODUCTION

This case was commenced by the Appellants under KRS 418.020 which permits a party to seek an advisory opinion on a legal question by alleging all facts upon which the legal question depends. The Appellants jointly sought to have draft regulations describing and instituting a particular patented gaming product declared not to violate Chapter 528 of the Kentucky Revised Statutes. To secure a favorable answer to their legal question, the Appellants concealed material facts upon which their legal question depended. The Franklin Circuit Court barred all pretrial discovery before a question was asked or an argument made. The Appellants appealed from an Opinion of the Kentucky Court of Appeals, entered June 15, 2012, which vacated the Opinion and Order, of the Franklin Circuit Court, entered December 29, 2010, finding that the Franklin Circuit Court abused its discretion by barring pretrial discovery.

## II. STATEMENT CONCERNING ORAL ARGUMENT

Appellee, The Family Trust Foundation of Kentucky, Inc., d/b/a The Family Foundation requests oral argument. Oral argument will (i) help insure that the Court has a complete understanding of the issues raised on appeal, (ii) afford the Court an opportunity to ask questions the Appellants refused to answer in the Franklin Circuit Court, and (iii) confirm that the Appellants are concealing material facts upon which their legal question depends.

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## IV. COUNTERSTATEMENT OF THE CASE

### A. Introduction.

The appellee, The Family Trust Foundation of Kentucky, Inc., d/b/a The Family Foundation (the "Appellee" or "The Family Foundation"), does not accept the statement of the case of the Kentucky Horse Racing Commission (the "Commission") in Appeal No. 2012-SC-416-D, the Kentucky Department of Revenue (the "Department") in Appeal No. 2012-SC-415-D, and the eight race track associations, Appalachian Racing, LLC, Churchill Downs Incorporated, Ellis Park Race Course, Inc., Keeneland Association, Inc., Kentucky Downs, LLC, Lexington Trots Breeders Association, Inc., Players Bluegrass Downs, Inc., and Turfway Park, LLC (sometimes referred to as the "Race Tracks") in Appeal No. 2012-SC-414-D. The Commission, the Department and the Race Tracks are sometimes collectively referred to as the "Appellants".

These appeals are from an Opinion of The Kentucky Court of Appeals, entered June 15, 2012, vacating the judgment of the Franklin Circuit Court finding that the Franklin Circuit Court abused its discretion by barring The Family Foundation from all pretrial discovery. The Court of Appeals remanded the case back to the Franklin Circuit Court for further proceedings, namely to allow The Family Foundation to conduct discovery and develop an evidentiary record. The Opinion of the Kentucky Court of Appeals vacating and remanding is attached as **Exhibit A**. After barring all pre-trial discovery, the Franklin Circuit Court issued an advisory opinion finding that the Commission's regulations describing the characteristics of an instant racing gaming product did not violate Chapter 528 of the Kentucky Revised Statutes. A copy of the Franklin Circuit Court Opinion and Order, entered December 29 2010, is attached as

**Exhibit B**. Franklin Circuit Court Record at Volume VI, page 793 - 810 (hereafter "TR __, __"). In its Opinion and Order, the Franklin Circuit Court also equated wagering on a 2" x 2" three second video display of a previously run horse race with wagering on live racing and declared that the wagers were subject to excise taxes on live racing under KRS 138.510(1). By Order, entered September 23, 2010, the Franklin Circuit Court declined to permit The Family Foundation to conduct any discovery whatsoever. A copy of the Franklin Circuit Court September 23, 2010, Order is attached as **Exhibit C**. TR IV, 599-601.

The Family Foundation seeks transparency and an objective regulatory process. The majority of the Court of Appeals, including former Justices of this Court, agreed. The Court of Appeals was unwilling to depart from the fundamental right of a party in litigation to ask questions and engage in pretrial discovery. The Court of Appeals was unwilling to adjudge this dispute with no evidentiary record whatsoever. The Court of Appeals was unwilling to give public agencies a blanket right to collude with their regulated entities with no questions being asked, no documents being reviewed and no devices being inspected. The Court of Appeals recognized that with the level of public interest in expanded gambling, complete transparency was required. The Court of Appeals also understood the negative perception arising from a case like this where public agencies collude with the entities they regulate to expand gambling without a vote of the people or of the General Assembly. The Court of Appeals vacated the actions of the Franklin Circuit Court.

## B. Summary of the Appeal.

On July 20, 2010, the Appellants purported to file an agreed case under KRS 418.020 which allows a party to seek an advisory opinion on a legal question if that party sets forth all facts upon which the answer to the legal question depends and explains the urgency of the need for such an answer. TR I, 1-192. Under KRS 418.020, the case is to be treated as an ordinary civil action. The legal questions in this case are (i) whether the Commission has the statutory authority under Chapter 230 of the Kentucky Revised Statutes to adopt regulations whereby the Commission may grant the Race Tracks licenses to host a new gaming scheme whereby patrons bet alone on a reel devices which also display a 2" x 2" video of a previously run horse race, and (ii) whether the Department has authority to tax it.

Chapter 528 of the Kentucky Revised Statutes prohibits all gambling and devices on which it is conducted, including pari-mutuel wagering. KRS 436.480 creates a narrow exception to the general prohibition by providing that "KRS Chapter 528 shall not apply to pari-mutuel wagering authorized under the provisions of Chapter 230." KRS 230.215(2) and KRS 230.361(1) define the Commission's statutory authority. What is and is not pari-mutuel wagering on legitimate horse racing under KRS 230.215(2) and KRS 230.361(1) is fact intensive. The Appellants set forth some facts upon which their legal question concerning the Commission's statutory authority depended, but concealed other material facts from the court.

The Appellants set forth virtually no facts in their joint petition, choosing instead to conceal the real characteristics of the patented gaming product proposed to be instituted by their regulations and refer only to assumptions, declarations and facts set

forth their draft regulations. Because of numerous deficiencies and omissions in the draft regulations, The Family Foundation needed discovery to make sure that all the facts upon which the Appellants' legal question depended were before the court. Otherwise, an answer to a hypothetical legal question without a record of facts upon which the question depended is a charade. Nonetheless, by barring all discovery the Franklin Circuit Court abused its discretion, denied The Family Foundation of due process under the 14th Amendment to the United Sates Constitution and violated of the separation of powers provisions under §§ 27 and 28 of the Kentucky Constitution. In sum, either the Appellants failed to set forth all facts upon which their legal question depended requiring the Franklin Circuit Court to be reversed and their joint petition to be dismissed; or, The Family Foundation was entitled to pretrial discovery to obtain facts in order for all the facts upon which the Appellants' legal question depended to be before the court requiring the Court of Appeals to be affirmed.

**C. Issues before the Court.**

This is not a case about the power of the courts to interpret a statute. This is a case about whether all the facts upon which the interpretation of a statute depend were before the court. Thus, the primary issue on this appeal is twofold: (a) does KRS 418.020 require all facts on which a hypothetical legal question depends to be before the court, and, if so (b) is it an abuse of discretion for a trial court to bar a party from all discovery of facts upon which the legal question depends. If all facts upon which the legal question depends do not have to be before a court and if a party to litigation may be barred from all pretrial discovery, then the issues on this appeal become much more complex,

requiring lots of assumptions, guessing and manipulation. A summary of these issues is as follows:

1. Does the Commission have the statutory authority to institute a gaming product which allows wagering on videos of previously run horse races on devices which otherwise display reels when patrons do not bet with or against each other on the same event or group of events?

2. If so, does the Commission have the statutory authority to institute a gaming product which allows wagering on videos of previously run horse races when patrons are not betting on a horse races, but instead on a 2" x 2" video display of a previously run horse race which appears on a reel device?

3. If so, does the Commission have the statutory authority institute a gaming product which allows wagering on videos of previously run horse races when material handicapping information is concealed?

4. If so, does the Department have the statutory authority to amend Form 73A100 to include reporting and taxing of wagering on videos of previously run horse races when its statutory authority to collect excise taxes is limited to wagering on live races?

**D. Proceedings in the Commission, The Franklin Circuit Court and the Court of Appeals.**

This case originated from a Commission meeting on July 20, 2010, at which the subject draft regulations were purportedly adopted. Commission Chairman, Robert Beck, stated:

> And historical racing is a term that we use. It's -- it's essentially the same thing or similar to instant racing in Arkansas. In the last Legislature there was a bill introduced on historical racing, and that bill was also unsuccessful. At -- when the -- when the failure to act on that bill became apparent, Governor Beshear asked the Racing Commission to investigate the possibility of historical racing in the State of Kentucky. At that point, the staff went into a due diligence mode, did a great deal of due diligence about the product, about the legal opportunity to -- to perform that product, the finances behind it and -- really just about -- just about every angle of this particular product. It took a great deal of time, a great deal of effort on the part of the staff.
>
> . . .
>
> At the conclusion of our due diligence, we had concluded that historical racing is a pari-mutuel wagering product and comes within the definition of pari-mutuel wagering and the Kentucky statute. And, that -- as a result, that we do have the power and we have the authority to promulgate regulations that would institute this product in the State of Kentucky. Once we reached the conclusion, the staff went to work drafting regulations.

See The Family Foundation Brief in Opposition to The Brief of (I) the Kentucky Horse Racing Commission, (II) the Kentucky Department of Revenue, and (III) the Eight Joint Petitioning Race Track Associations, Exhibit G -- Transcript of Meeting of the Racing Commission, July 20, 2010, pp. 5-6, TR V.[1] Because the General Assembly failed to pass a necessary bill in the 2010 Session which would have allowed the instant racing product, the Commission sought to do so by regulation. The Commission first analyzed the instant racing product after which the Commission drafted regulations to institute the product. According to the fiscal note attached to the draft regulations the product was the same product hosted by Oaklawn Park in Hot Springs, Arkansas. Draft Regulation, 810 KAR

[1]The Family Foundation Brief in Opposition did not appear to be included in the numbered pages of the trial court record. References herein will be to the pages of the brief itself.

1:011, p. 27. Oaklawn Park describes the instant racing devices as reel games.[2] On July 20, 2010, the Commission adopted the draft regulations with no discussion and no dissenting vote. On July 20, 2010, the Department amended its excise tax reporting and collection Form 73A100 to collect excise taxes on the new instant racing product.

In addition to the Chairman's admissions, the Commission's actions confirm that this case is about a particular gaming product. On page 2 of the Commission's reply brief in the Franklin Circuit Court, the Commission admitted that instant racing is a "trade name and refers to a specific, trademarked product offered by RaceTech, LLC, through which wagering on historical racing can be conducted." TR V, 643. By Commission redacted and undated email from Greg Lamb to wkoski@spike.dor.state.co.us, it was stated: "Kentucky is considering INSTANT RACING machines which are somewhat similar to slot machines and we would like someone to check their integrity." [Emphasis in original]. TR. V, 739. By email, dated January 14, 2010, from Greg Lamb to Lisa Underwood, entitled "'Instant Racing' Canada", it was stated by Mr. Lamb: "I just talked to my contact in Canada and he said no tracks have approached the Authority there to request the use of 'Instant Racing' machines. He said they have looked at the concept of the machines, and they feel they would not fall under their pari-mutuel regulations mainly due to the use of taped events." TR V, 735. The Commission's press release proclaimed approval of the proposed regulations "to allow 'Instant Racing' wagers at tracks" TR V, 738. By email, dated January 6, 2010, from Greg Lamb to Commission Executive Director, Lisa Underwood, with the subject "Arkansas rules", it was stated: "The rules for

[2]KRS 528.010(4)(a) prohibits reel games.

Instant Racing are 91 pages long." TR V, 731. By email, dated January 7, 2010, from Commission Chairman, Robert Beck, Jr., to Lisa Underwood, it was stated "Lisa-I've got a few thoughts about Instant Racing." TR V, 733. By email, dated July 8, 2010, from Lisa Underwood, private meetings appear to have been arranged and conducted on July 14, 2010, in both Louisville and Lexington pertaining to the regulations. TR VI, 765, 767. A July 19, 2010, an email from the Kentucky Equine Education Project was sent to advocates, including members of the Commission, announcing that "The Commission is expected to pass regulations allowing for pari-mutuel wagering on historical races, or 'Instant Racing' as it is more commonly referred to. The passage of Instant Racing will provide some much needed good news for our industry. The meeting is open to the public, so please feel free to attend. We will have an in-depth discussion of Instant Racing at our Board Meeting on Thursday morning." TR VI, 769.

Following the Commission's adoption of the draft regulations on July 20, 2010, on the same day, the Appellants filed a joint agreed case in the Franklin Circuit Court under KRS 418.020 in which they named only themselves, with no defendants and no respondents.[3] Accompanying their joint petition were ten affidavits from representatives of each of the joint petitioning Appellants in nearly identical form, four of which were executed on July 19, 2010, before different notaries, -- the day before the meeting -- strangely attesting to events which had not yet occurred. Six days after the agreed case was filed, without a motion, a hearing or any supporting evidence in the record, by Order,

[3]The Appellants could have named the Justice Cabinet, the Kentucky State Police or a Commonwealth Attorney to present the other side of the issue, but strangely did not. Law enforcement may not have been willing to go along with the *plan*.

entered on July 26, 2010, the Franklin Circuit Court *sua sponte* set a date for the Appellants to file briefs and, in so doing, also made nearly three pages of evidentiary findings about the case, with no evidence in the record, including a declaration that the case presented a justiciable controversy under KRS 418.020.[4] TR II, 193-197.

On August 23, 2010, The Family Foundation filed a motion to intervene which was unopposed. TR V, 201-203, 204-253. By Order, entered September 2, 2010, the Franklin Circuit Court allowed The Family Foundation to become a party [TR IV, 476-478]; but again, with no motion before the court, the Franklin Circuit Court ordered The Family Foundation to file its brief by October 1, 2010 -- in 29 days, with no opportunity for discovery. TR IV, 479-481. On September 14, 2010, The Family Foundation filed a response to the joint petition in which it denied the allegations in the joint petition and asserted affirmative defenses, including failure to comply with KRS 418.020. TR IV, 491-99. Also on September 14, 2010, The Family Foundation filed a motion to modify

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[4]That Order may have been drafted by a clerk/staff attorney for the trial court with independent knowledge such that facts and evidence were believed to be unnecessary. The current professional biography of one of the trial court's clerks/staff attorneys at the time indicates a membership in the Kentucky Equine Education Project (KEEP), a leading advocate for expanded gambling. The president of appellant, Kentucky Downs, LLC, is/was the Chairman of KEEP. Kentucky Downs, LLC, was the first applicant for a license and the first track to install the instant racing devices. The July 19, 2010, email, referenced above, confirms KEEP's involvement in the regulatory process. KEEP also presented on May 10, 2011, in support of the instant racing regulations at the Administrative Regulation Review Subcommittee of the Legislative Research Commission. The transcript of the December 14, 2010, hearing confirms the clerk's presence. Copies of the clerk's professional biographies indicating that she drafted orders and opinions for the trial court and referencing a current membership in KEEP can be provided. Her 2013 publication on instant racing in Kentucky in *Casino Lawyer* magazine and her 2008 article in the New York Times horse racing blog, The Rail, can also be provided. The Court may take judicial notice of the court's employees and possible reasons supporting evidence was deemed unnecessary. This is likely a strange coincidence which can be explained and certainly nothing improper is being alleged or implied at this time.

the second September 2, 2010, *sua sponte* Order to allow it to conduct pretrial discovery. TR IV, 482-485, 599-570. Notwithstanding admissions by the Chairman of the Commission that that the regulations were drafted to conform to a particular product, that the draft "regulations would institute this product", the staff's use of reel games at Oaklawn Park for the Commission's impact statement and a host of email traffic about instant racing, the Appellants insisted that all facts about the product upon which their legal question depended were irrelevant and inadmissible and therefore not subject to discovery. Although there was no motion for a protective order and with the court asking its own factual questions, the Franklin Circuit Court agreed and by Order entered September 23, 2010, held that all questions before it were legal questions and barred The Family Foundation from all discovery.[5] TR IV, 600. Strangely, the Franklin Circuit Court could not have known that the questions before it were purely legal questions because The Family Foundation had not yet made an argument. The Franklin Circuit Court could not have known whether discovery that might have been sought by The Family Foundation would be irrelevant and inadmissible because The Family Foundation had not yet asked a question. Like the July 26, 2010, Order, the extraordinary action to bar all discovery defies explanation from the record except for the court's expression of regret of allowing The Family Foundation to intervene: "[T]o tell you the truth, if they [the Appellants] had objected, I would have probably not allowed you [The Family Foundation] to be a party, but I would have allowed you [The Family Foundation] to do an amicus." Franklin Circuit Court Video Record, September 20, 2010, Video Reference ("VR") 48-2-10-VCR-31, time references do not appear. A copy of the relevant page of

[5]See footnote 4.

the transcript is attached as **Exhibit D**. The Appellants did not object to The Family Foundation's intervention. They needed The Family Foundation in the case to cure the ripe controversy requirement. They just had to be sure The Family Foundation asked no questions.

With The Family Foundation securely gagged, blindfolded and unable to develop an evidentiary record of facts on which the Appellants' question depended on December 29, 2010, the Franklin Circuit Court entered an Opinion and Order summarily granting the Appellants' joint petition for declaratory judgment. TR VI, 793-810. The Family Foundation appealed to the Kentucky Court of Appeals. This Court unanimously denied the Appellants' motion for expedited review.

Even though the Opinion and Order of the Franklin Circuit Court was not final, the Commission proceeded to approve an application from Appellant, Kentucky Downs, LLC, to install the instant racing product just as the Chairman of the Commission said it would do at the July 20, 2010, meeting. The Family Foundation moved the Court of Appeals for intermediate and emergency relief and an injunction to enjoin Appellant, Kentucky Downs, LLC, from proceeding with the installation and operation of the instant racing devices. The Family Foundation attached to its motion photographs of the instant racing devices installed at Kentucky Downs, LLC. The Court of Appeals granted The Family Foundation's motion for an emergency hearing at which time the photographs of the gaming devices became part of the record in the Court of Appeals. The photographs make clear that when the Chairman of the Commission indicated that the regulations that would institute this product, he was referring to video slot machines. Appellant, Kentucky Downs, LLC, opposed the motion for an injunction on the grounds that KRS

501.070(3)(a)-(c) permitted it to avoid criminal prosecution because it acted in reliance on an order of a court and approval by the Commission. The Court of Appeals denied the request for an injunction, but, like The Family Foundation, was unaware at the time of additional questions concerning the legitimacy of the actions of the Franklin Circuit Court. The Family Foundation eventually prevailed in the Court of Appeals on the underlying appeal in which the Opinion and Order of the Franklin Circuit Court was vacated. On January 11, 2013, the Appellants' petitions for discretionary review to this Court were granted.

**E. Skepticism Is Merited.**

The proceedings in the Franklin Circuit Court could only be described as bizarre. A healthy skepticism is justified by (i) a joint agreed case among public and private entities seeking immunity from criminal prosecution for activities and devices to be instituted by regulations which were adopted with no discussion *after* the General Assembly had failed to pass a bill authorizing the activity, (ii) followed by *sua sponte* Orders reciting evidence which is not in the record, (iii) the barring of all discovery before a question was asked, and (iv) the complete absence of witnesses testimony and evidence in the record. This is not the first time instant racing proponents have attempted to trick a court of justice. In *Wyoming Downs Rodeo Events, LLC, et al., v. State of Wyoming et al.*, 134 P.3d 1223 (Wyo. 2006), the *Wyoming Downs* court concluded its rejection of a claim that the instant racing product was pari-mutuel wagering, stating: "Although it may be a good try, we are not so easily beguiled." *Wyoming Downs Rodeo* at p. 1230. Similarly addressing the instant racing product, the court in *MEC Oregon Racing, Inc. v. Oregon Commission*, 225 P.3d 61, 67 (Or. App. 2009), found that "There

are no mutuel pools for the specific races. Instead, the pool consists of players betting on any of the 20,000 different races that took place in the past at various times and places. Thus, there are no mutuel pools for the races at the race course, as ORS 462.720(1)(b) requires." By opinion, dated March 17, 2009, the Maryland Attorney General found that instant racing was not pari-mutuel wagering:

> By contrast, with Instant Racing, wagers on completely different races are pooled together based only on the various types of 'wins' available to all the players. Instead of each betting pool being shared by all of those who selected the correct order of finish in a particular race, the Instant Racing winner takes all of the money that has accumulated in the applicable betting pool at the time of that person's successful bet. . . .
>
> Furthermore, bettors in a traditional pari-mutuel system, through their differing opinions and the money wagered on such opinions, participate directly in setting the odds on the various possible outcomes of a given race. Typically, the bettors are the only determinant of what the odds will be. For obvious reasons, this cannot occur in Instant Racing because, as noted above, no two players are ever betting on the same race.

**F. The Subject Regulations.**

For years, proponents of expanded gambling have poured millions of dollars into campaigns attempting to secure the election of favorable legislators, attorneys general[6] and governors, and through that, enough votes and influence to expand casino-style gambling in Kentucky by constitutional amendment, by statute and, most recently, by regulation. To date, they have not been successful by constitutional amendment or by

[6]On January 5, 2010, the Attorney General of Kentucky opined that the only obstacle he believed stood between expanded gambling in the form of instant racing *under the pari-mutuel statute* were the existing regulations of the Kentucky Horse Commission. Opinion of the Attorney General, p. 1. The Attorney General's January 5, 2010, opinion was qualified, however. In the first footnote, he stated: "If regulatory or statutory changes are considered to permit this sort of wagering, the proponents should also be cognizant of the requirements of KRS Chapter 528 with regard to 'gambling devices' and consider whether amendments to that chapter are also in order", i.e., videos are not horse races.

statute. As the Commission Chairman Robert Beck pointed out, the Commission started the process of promulgating the subject regulations only after the 2010 Session of the General Assembly refused to pass a bill allowing instant racing. That being the case, the effort was taken to the regulatory agencies and the courts where two public state agencies and eight private race track associations proceeded to try to accomplish *indirectly* which they were unsuccessful in accomplishing *directly*. To this end, on July 20, 2010, the Commission adopted nine sets of amendments and new regulations, the primary purpose of which was to authorize and institute the installation of video slot machines, also known as instant racing. On the same day, the Appellants filed a joint petition seeking an advisory opinion from the Franklin Circuit Court that the regulations that would institute the instant racing product were legal and did not violate Chapter 528 of the Kentucky Revised Statutes. The new Regulations were referenced as being attached to the joint petition as Exhibit A. The new Regulations were attached as Exhibit B to The Family Foundation's Brief in Opposition to the Brief of (I) The Kentucky Horse Racing Commission, (II) The Kentucky Department of Revenue, and (III) the Eight Joint Petitioning Race Track Associations, filed on October 15, 2010, TR V, (the "Regulations"). Citations to the new Regulations are as follows:

Thoroughbred:

810 KAR 1:001 – Definitions, amendments
810 KAR 1:011 – Pari-Mutuel Wagering, amendments
810 KAR 1:120 – Exotic Wagering, new

Standardbred:

811 KAR 1:005 – Definitions, amendments
811 KAR 1:125 – Pari-Mutuel Wagering, amendments
811 KAR 2:250 – Exotic Wagering, new

Quarter Horse, Appaloosa, Arabian

811 KAR 2:010 – Definitions, amendments
811 KAR 2:060 – Pari-Mutuel Wagering, amendments
811 KAR 2:160 – Exotic Wagering, new

**G. Factual Questions In Search Of Answers.**

The joint petition, eleven affidavits,[7] trial court's questions, the Race Tracks' participation as a party in the case and the Regulations themselves raise a host of factual questions, not only by what was said but significantly by what was not said. Surely, anyone who looks at this case can see what is really going on. Even though the Appellants insist on total and complete secrecy, the Franklin Circuit Court stated that someone was going to have to explain to him what instant racing was all about -- a fact upon which the Appellants' legal question depended: "Yeah, I want somebody to eventually tell me what this stuff is about, you know, this instant racing." Video Record, September 20, 2010, 48-2-10-VCR-31, no time tracking appeared on the video record. A copy of the page of the Transcript is attached as **Exhibit E**. TR VI, 844. Yet, no one did on the record. The Franklin Circuit Court also wanted to know how the odds were calculated for the instant racing game -- another fact upon which the Appellants' legal question depended. "The payoff would be the same as it was on the date [of] the historical race?" Video Record, December 14, 2010, 48-2-10-VCR-39 at 11:00:24-28. A copy of the page of the Transcript is attached as **Exhibit F**. TR VI, 847. Yet, no one did on the record. The Commission Chairman said these are the "regulations that would

[7] The eleventh affidavit was tendered by the Commission in support of its motion for declaratory /summary judgment.

institute this product." Yet the Appellants insist that nothing may be known about the product or the Regulations.

Facts were concealed upon which the answer to the Appellants' legal question depended. For example: The formula for calculating the odds was not disclosed. The person or machine who/which determines payouts was not disclosed. How a person can handicap a video without handicapping information was not disclosed. How videos with names, races, owners, trainers concealed can be legitimate horse races was not disclosed. That a "trivial pool of one" could not be a pari-mutuel pool was not disclosed. The person or machine who/which collates the "trivial pools of one" was not disclosed. The real reason the question was immediate was is not disclosed. The facts justifying a seven month delay of review by the legislative committee was not disclosed. How the reel devices at Oaklawn Park were not reel devices in Kentucky was not disclosed. What private Commission meetings on the Regulations were conducted prior to the July 20, 2010, meeting as four of the sworn affidavits suggest, was not disclosed. The location of ticket windows and how winning tickets are cashed was not disclosed. If a video of a horse is actually a horse, where you feed it and if it will get out if the gate is open was not disclosed. Whether a better with an IQ greater than plant life exists who cannot tell the difference between (i) betting on gambling device which displays a 2" x 2" three second video of an old horse race and (ii) wagering on live legitimate horse race was not disclosed. The Appellants argue that the bet of a patron on a gambling device who cannot tell that it is not a live horse race is subject to excise tax, but the Appellants do not disclose whether the wager of a patron who can tell the difference is subject to tax. With all this information being concealed, the Appellants still claim that they may not be asked

for one single item of information upon which their question depended and are still entitled to have the game declared legal. Surely justice in Kentucky has not come to this.

## V. ARGUMENT

Only one of three outcomes is legally possible here under current law. First, pretrial discovery was arbitrarily denied, requiring the Court of Appeals to be affirmed. Second, the requirement under KRS 418.020 that all the facts be alleged upon which a legal question depends was not satisfied requiring the case to be dismissed. Third, based on the limited facts which are known, the Regulations and the product they purport to institute are outside the scope of the Commission's authority to implement and the Department's authority to tax.

### A. Denial Of All Pretrial Discovery Was An Abuse Of Discretion.

The Family Foundation was entitled to conduct discovery on all facts upon which the Appellants' legal question depended. Information about the allegations in the joint petition, the affidavits, the questions the Franklin Circuit Court asked, the Regulations themselves, potentially undisclosed relationships and the predated affidavits is and was discoverable. It cannot be credibly argued that all information about the products, games and devices the Commission intended to institute and which the Race Tracks intended to fund, apply for, install, operate and host which are purportedly described in the Regulations is not relevant, admissible or discoverable. Under KRS 418.020, the Appellants were required to affirmatively disclose all the facts upon which their legal question depended. Because they did not, The Family Foundation needed to conduct discovery to do so itself. Yet, the Appellants opposed that. The concern could not have been about delay or expense. The Appellants delayed a hearing by the Administrative

Regulation Review Subcommittee for seven months. Even with this appeal pending, Appellants were not dissuaded from approving licenses and installing devices. So, what could it be? If the Appellants are so confident that the instant racing product is the same thing as pari-mutuel wagering on legitimate horse races and therefore legal, and that their hypothetical legal question would be answered in the affirmative, what are they so desperate to hide?

**1. Rule 26 Allows Parties To Conduct Discovery.**

Under Kentucky law, parties are entitled to conduct pretrial discovery as a matter of right. Kentucky Rule of Civil Procedure 26.02(1) provides that:

> Parties may obtain discovery regarding any matter, not privileged, which is relevant to the subject matter involved in the pending action, whether it relates to the claim or defense of the party seeking discovery or of the claim or defense of any other party, including the existence, description, nature, custody, condition and location of any books, documents, or other tangible things and the identity and location of persons having knowledge of any discoverable matter. It is not ground for objection that the information sought will be inadmissible at the trial if the information sought appears reasonably calculated to lead to the discovery of admissible evidence.

When the Appellants availed themselves of the courts by filing their agreed case, they likewise agreed to allege all facts upon which their legal question depended and abide by the Rules of Civil Procedure. The only exception to the broad practice of discovery in Kentucky is under Civil Rule 26.03 which allows discovery to be limited upon motion and for good cause shown. Only in such an event may a court make an order to protect a party or person from annoyance, embarrassment, oppression, or undue burden or expense. No motion was made in this case. Moreover, no one was annoyed, embarrassed, oppressed or unduly burdened or caused unnecessary expense because discovery was

barred before any questions were asked and before any arguments were made. The Franklin Circuit Court abused its discretion by barring all discovery in this case especially when necessary facts upon which the Appellants' legal question depended were being concealed.

This Court has previously cautioned that: "Until the time of trial *every litigant must have the opportunity to search for and secure whatever evidence may be necessary to perfect his case,* and unless it is manifestly impossible for him to produce it he cannot be forced to a premature showdown in that respect by a motion for summary judgment." [Emphasis added]. *Roberson v. Lampton*, 516 S.W.2d 838, 839-849 (Ky. 1974), citing *Payne v. Chenault*, 343 S.W.2d 129, 132 (Ky. 1961). Since The Family Foundation was a litigant, it had the right to search for and secure evidence necessary to perfect its case, including the right to make sure that all facts upon which Appellants' legal question depended were before the court before a premature summary/declaratory judgment.

The Appellants attempt to justify the barring of all discovery saying that all information about the Regulations and the product they would institute is irrelevant and therefore inadmissible. KRS 418.020 makes all facts upon which the legal question depends relevant and admissible because they are required to be alleged in the filing with the court. Even if that was not required, relevancy and admissibility are not the standards for determining whether pretrial discovery is allowed under Civil Rule 26. Nowhere does Civil Rule 26 contemplate that pretrial discovery may be barred because the evidence is inadmissible. Quite to the contrary, evidence only needs to be reasonably calculated to lead to the discovery of admissible evidence to be discoverable. *Ewing v. May*, 705 S.W.2d 910 (Ky. 1986). To this end, pleadings are the touchstone by which the subject

matter of an action is determined. *Carpenter v. Wells*, 358 S.W.2d 524 (Ky. 1962). In this case, the facts upon which the question depends (KRS 418.020) are purportedly set forth in the joint petition, affidavits, opinion of the attorney general and the Regulations themselves. A fundamental requirement of KRS 418.020 is that all facts upon which the question depends be stated. That has not been done. Under no constitutional authority may a party be barred from asking questions about facts upon which a legal question depends in any civil action. Yet, that is precisely what the Appellants insist be done.

**2. KRS 418.020 Requires All Facts As If In An Actual Civil Action.**

Assuming KRS 418.020 is constitutional,[8] it allows parties to file an agreed case to seek an advisory opinions on a question, provided the party(ies) include a complete statement of facts upon which the question depends:

> Parties to a question which might be the subject of a civil action may, without action, state the question and the facts upon which it depends, and present a submission thereof to any court which would have jurisdiction if an action had been brought. But it must appear by affidavit that the controversy is real, and the proceedings in good faith, to determine the rights of the parties. The court shall, thereupon, hear and determine the case, and render judgment as if an action were pending.

The requirement of "the facts" requires a complete and truthful statement of all facts upon which the question depends. Allowing parties to obtain an advisory opinion based on alleged facts which are false, incomplete, omitted or subject to further finding by a third party would work a fraud upon the court whose advice is sought. KRS 418.020 is not a statute to be manipulated. The whole point of KRS 418.020 is to get all the facts before the court, both good and bad, and treat the case as if an action was pending so that the

[8] It is not the function of the courts to render advisory advisory opinions. *Dravo v. Liberty National Bank*, 267 S.W.2d 95 (1954).

advisory answer to the question is based on a complete and truthful record. Treating the case as something different than an actual civil proceeding as the Appellants insist would obviously deprive the answer of legitimacy and unquestionably result in KRS 418.020 being an unconstitutional advisory opinion. *See e.g., Nordike v. Nordike*, 231 S.W.3d 733, 739 (Ky. 2007); *Dravo v. Liberty National Bank*, 267 S.W.2d 95 (Ky. 1954); *Black v. Elkhorn Coal Corp.*, 26 S.W.2d 481, 483 (Ky. 1930).

The question here is whether the activity, conduct and devices described by the joint petition and in the Regulations, constitute pari-mutuel wagering on legitimate horse racing under Chapter 230, specifically under KRS 230.315(2) and 230.361(1), so as to be within the exception to the prohibition in Chapter 528 against gambling allowed by KRS 436.480. To answer their hypothetical question, however, complete, unbiased, truthful and accurate facts are required to be stated under KRS 418.020. Anything less, an advisory answer to the hypothetical question becomes a farce. The joint petition and the Regulations here omit material facts, state incomplete facts and purport to include facts which are mutually exclusive to pari-mutuel wagering on legitimate horse racing allowed by Chapter 230. For example, nowhere is wagering pool or net pool defined as a matter of fact. Nowhere is the fact disclosed that historical racing consists of a "trivial pool of one" arising from a wager on a "unique event" which is mutually exclusive to pari-mutuel wagering. Nowhere is the fact disclosed under historical racing wagerers are not wagering with and against each other, another fact mutually exclusive to pari-mutuel wagering. Nowhere is the fact disclosed that wagerers are not wagering on a legitimate horse race. Nowhere are facts disclosed about how odds are calculated and payouts are determined. Nowhere is the fact disclosed that it is impossible for a wagerer on a

historical horse race to be competing with other wagerers on the same or similar group of events since patrons are not betting with and against any other wagerer. Nowhere is the fact disclosed that pari-mutuel odds cannot be calculated on a race that has already occurred and in which there is only a single participant. Nowhere is the fact disclosed that a totalizator cannot calculate new odds on a race that was already run. Nowhere is the fact disclosed that it is impossible to calculate odds on races in which there are no wagerers betting against each other. Nowhere is the fact disclosed that a totalizator cannot logarithmically calculate the odds of winning or the payout on straight or exotic wagering on combinations of thousands of randomly selected videos of previously run horse races made at various times by different bettors at various locations. Nowhere is the fact disclosed that a totalizator cannot calculate the size of the mutuel pool required to payout the winnings on all the combinations of straight or exotic wagers on every combination of 22,000 randomly selected videos of previously run horse races made at various times by different bettors at different locations through instant racing devices.

The need for complete factual information to answer the Appellants' question does not stop there. The thoroughbred and quarter horse regulations purport to define "Race" as "a running contest between horses, ridden by jockeys, over a prescribed course free of obstacles or jumps, at a recognized meeting, during regular racing hours, for a prize." 810 KAR 1:001, Section 1(59); and 811 KAR 2:010, Section 1(70). "Race" is not defined in the standardbred regulations. 811 KAR 1:005. The fact that a "Race" under instant racing includes videos of dead horses, undisclosed jockeys on an undefined course at an unnamed meeting is undisclosed.

Similarly, the thoroughbred regulations define "horse" as "a thoroughbred registered with The Jockey Club and when used in these administrative regulations, any thoroughbred irrespective of age or sex designation." 810 KAR 8:001, Section 1(33). The standardbred regulations define "horse" as "any equine (including and designated as mare, filly, stallion, colt, ridgeling, or gelding) registered for racing." 811 KAR 1:005, Section 1(45). The quarter horse regulations define "horse" as "a quarter horse, appaloosa or Arabian registered as such with the American Quarter Horse Association in Amarillo, Texas, or the Appaloosa Horse Club, Inc., in Moscow, Idaho; and when used in these rules to designate any quarter horse, appaloosa or Arabian irrespective of age or sex designation." 811 KAR 2:060, Section 1(39). That the Appellants equate "horse" to a video or a movie is an undisclosed fact. That breed associations do not register videos or a movies of dead horses is an undisclosed fact.

The Regulations provide that a "historical horse race" is defined as "any horse race that was previously run at a licensed pari-mutuel facility located in the United States and that concluded with official results. An historical horse race must have concluded without scratches, disqualifications, or dead-heat finishes." 810 KAR 1:001, Section 1(32); 811 KAR 1:005, Section 1(44); and 811 KAR 2:010, Section 1(38). That historical horse race includes movies and videos displayed on a reel device in instant racing about which the Kentucky Attorney General was concerned is a material but undisclosed fact.

The Regulations purport to define "terminals" as "any self-service totalizator machine or other mechanical equipment used by a patron to place a pari-mutuel wager on a live or historical horse race." 801 KAR Section 1, 1:001(77); 811 KAR Section 1, 1:005(87); and 811 KAR Section 1, 2:010(93). The Regulations define "totalizator" as

"the system, including hardware, software, communications equipment, and electronic devices that accepts and processes the cashing of wagers, calculates the odds and prices of such wagers, and records, displays, and stores pari-mutuel wagering information." 810 KAR 1:001, Section 1(79); 811 KAR 1:005, Section 1(88); and 811 KAR 2:010, Section (94). That a totalizator cannot calculate odds on a race in which there is only a single participant and cannot calculate new odds on a previously run race are undisclosed facts.

The question the Appellants themselves have asked is directly dependent on the truthful and complete answer to these factual questions. Yet, the Appellants insist that these facts are irrelevant, inadmissible, not discoverable must remain concealed. Discovery should also have been allowed on the allegations in the joint petition. Paragraph 14 refers to the instant racing gaming scheme which was contemplated in the 2010 Opinion of the Kentucky Attorney General. Facts pertaining to the patented gaming product described by the Kentucky Attorney General are facts upon which the Appellants' question is based. If not, why was the Opinion attached to the joint petition? The factual basis for the Commission Chairman's announcement that the Commission had the "power to promulgate regulations that would institute this product" are facts upon which the Appellants' question is depends. Paragraph 19 of the joint petition alleges "immediate and prominent issues of public concern". Facts constituting "immediate" and "prominent issues of public concern" are undisclosed. Paragraph 19 of the joint petition alleges that instant racing may "generate additional tax revenue". Information supporting this belief and allegation are discoverable. Information about how much additional revenue, how many machines, revenue per device are all potential facts upon which the Appellants' legal question is based but are concealed. Whether a patented instant racing

gaming product could generate additional tax revenue if it is not "live racing" is a fact upon which the Appellants' question is based. Paragraph 19 alleges that instant racing would improve the "financial viability" of the horse industry. How it would do that and upon what gaming device/product would improve the financial viability of the horse industry are facts upon which the Appellants' legal question is based but were not disclosed.

Paragraph 20 of the joint petition alleges that "The Associations will be required to make a substantial financial commitment in order to offer pari-mutuel wagering on historical horse racing, including the purchase, installation, and approval of new terminals." The instant racing gaming product the Race Tracks intend to offer is a material undisclosed fact upon which the Appellants' question is based. In paragraph 20 the Appellants allege that "Before making this investment, the Associations need to confirm: (1) the validity of the Regulations (to insure that they may proceed without being subject to any legal penalties, including criminal liability under Kentucky's penal code), and (2) the proper form of taxation for wagering on historical horse races." Information about the product in which the Race Tracks intend to invest and how much they intend to invest are material facts upon which the answer to the Appellants' legal question depends but which was concealed. The Race Tracks are parties to this case which are seeking an advisory opinion about future conduct making their intentions factually relevant to the question they have asked.

In subparagraph (b), of paragraph 22 of the joint petition, the Appellants allege that they are seeking a determination that: "The licensed operation of pari-mutuel wagering on historical horse races, as authorized by the Regulations, does not contravene

statutory prohibitions on gambling contained in Chapter 528 of the Kentucky Revised Statutes, because it is an authorized form of pari-mutuel wagering exempted pursuant to KRS 436.480." Factual information about what "it" is is a fact upon which the Appellants' legal question depends. Information about what the Race Tracks are going to purchase and install are undisclosed facts about which the Appellants' legal question depends. Information about the activities the Appellants are concerned may expose them to criminal penalties are undisclosed facts upon which the Appellants' legal question depends.

There are obvious additional facts upon which the Appellants' legal question depends which are not disclosed. For example, The formula by which odds are set and payouts determined is undisclosed. If such a formula exists, how it works was undisclosed. The Commission performed extensive due diligence which had to reveal facts upon which the Appellants' legal question depended, yet nothing about the due diligence was disclosed. The facts which caused the Appellants to have so much doubt about the Regulations that an agreed case was required under KRS 418.020 was not disclosed. Truthful, complete and factual answers to these questions are facts upon which the answer to the Appellants' legal question depends but which were concealed.[9]

[9]A third alternative is possible. The intervention of The Family Foundation took the case outside of the purview of KRS 418.020 and made it an ordinary civil proceeding for a declaratory judgment. If so, then The Family Foundation has all the pretrial discovery rights of a party to a civil action under the Kentucky Rules of Civil Procedure. Regardless of the scenario, the case has to be dismissed for failure to comply with KRS 418.020, KRS 418.020 is unconstitutional or The Family Foundation has the absolute right to conduct pretrial discovery.

Other than the Department's hypothetical wagerer who cannot tell the difference between pumping quarters in a video slot machine and a placing wagers on a live horse race, the Race Tracks' argument that "This case has never been an "as applied" case is perhaps the most frivolous of all the arguments advanced by the Appellants. Race Tracks Appellate Brief, p. 8. All the facts upon which the legal question depends are required to be applied, including facts which support the desired outcome and facts which mitigate against it. That is the expressed condition of the statute. The whole point of an agreed case under KRS 418.020 is for facts to be applied to a hypothetical legal question. As a result all questions under KRS 418.020 are "as applied". Otherwise, the advisory answer is of no value whatsoever because it was not a product of actual facts. This argument admits, however, that the facts applicable to the question were not applied because they were not before the court.[10] Without applied facts, the Appellants concede that the Commission was wrong to rely upon the Franklin Circuit Court's Opinion and Order.

**B. *McConnell v. Commonwealth* Was Different.**

The Kentucky Supreme Court has repeatedly mandated trial courts not to decide speculative rights or duties of parties that may or may not arise in the future. *Nordike v. Nordike*, 231 S.W.3d 733, 739 (Ky. 2007)(additional citations omitted); *Black v. Elkhorn Coal Corp.*, 26 S.W.2d 481, 483 (Ky. 1930).[11] Ignoring the admonitions of this Court, the

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[10]Given this, none of the Appellants have a basis to rely on the Opinion and Order of the Franklin Circuit Court and are not immune under KRS 501.070(c).

[11] *Chambers v. Stengel*, 37 S.W.3d 741 (Ky. 2001), is inapplicable. It involved certification of a question of law: "This case comes to this Court on a request for a certification of law from the United States Court of Appeals for the Sixth Circuit." *Id.* at 742. In the case before the Sixth Circuit Court of Appeals there was a real controversy.

Franklin Circuit Court proceeded with the case, saying that an advance determination would eliminate the risk of future wrongful action and attempted to apply *McConnell v. Commonwealth*, 655 S.W. 2d 43 (Ky. App. 1983).[12] This case is not like *McConnell,* however. Because of that, under the foregoing authority, the Franklin Circuit Court was without constitutional authority to act.

In *McConnell*, parties were seeking an advance declaration that a new "infrared evidential breath tester" qualified as a breath tester for purposes of determining blood alcohol content. Before making the investment of public funds in new "infrared equipment", the parties wanted to be sure the evidence collected by the infrared equipment would be admissible evidence as a "chemical test" under Chapter 186 of the Kentucky Revised Statutes. The *McConnell* court had an actual evidentiary record in which witnesses explained the new infrared equipment and the infrared equipment itself was evaluated. The proponents alleged all facts upon which the legal question depended. The *McConnell* decision was "based on evidence". *Id.*, at 46. In this case, the Appellants have not provided nor produced any evidence of facts upon which their question depends.

*McConnell* also required that a party be reluctant to act. There was no reluctance to act here. The Commission adopted the draft regulations and has since approved three applications for instant racing devices under the Regulations. Two Race Tracks have also acted and have and/or are installing nearly 500 instant racing video slot machines, even with an appeal pending. The Appellants propose a different application of KRS 418.020,

[12]The Appellants' failure to comply with KRS 418.020 was not addressed in the December 2010 Memorandum Opinion except to say that with no motion, no hearing and no evidence the Court held that the case was "justiciable controversy" in its July 26, 2010, *sua sponte* Order and it was not going to reconsider that holding.

where only limited favorable facts upon which the question depends are presented, and all other facts are concealed. Unlike in *McConnell*, the Appellants here offered no witness testimony, no exhibits, not even the devices contemplated by the Regulations were inspected. In their "as applied" argument, the Appellants even concede that their question is not applied to any facts. And that is precisely what they want. Unlike *McConnell*, where the parties wanted a factual record to support the answer to the legal question, the Appellants opposed any factual record. Suffice it to say that if the Appellants are so sure fire positive that the patented instant racing product the Regulations propose to institute is not illegal why would they care what pretrial discovery would show? What on earth are the Appellants so afraid will be discovered? Why the need for a cover-up? Why would the Appellants so vigorously oppose a factual glimpse into what they are doing if it is legal? Of course, everyone knows why it is just a matter of discovery to show it.[13]

**C. Summary/Declaratory Judgment Was Premature.**

The Franklin Circuit Court entered judgment with no evidentiary record, undisclosed facts upon which the legal question depended and material factual questions, including factual questions which the court itself asked. Not one single witness was called or document introduced. The devices themselves were kept secret. Under Kentucky law, no judgment is to be entered until after discovery is complete. Trial courts "are to refrain from weighing evidence at the summary judgment stage; that they are to review the record *after discovery has been completed* to determine whether the trier of

[13] Luke 12:2-3 (KJV).

fact could find a verdict for the non-moving party." [Emphasis added]. *Welch v. American Publishing Co.*, 3 S.W.3d 724, 729 (Ky. 1999). Even if facts tend to favor the moving party, on a motion for summary/declaratory judgment, all inferences must be drawn in favor of the party against whom the motion is directed. *Mitchell v. Jones*, 283 S.W.2d 716, 718 (Ky. 1955). Even if a small doubt as to the existence of an issue of fact, a litigant against whom summary judgment is sought has a right to a trial where there is a doubt about the facts. *Simpson v. Graves*, 451 S.W.2d 399, 401 (Ky. 1970).

The Franklin Circuit Court's barring all discovery and entering judgment for the Appellants violated well-known directives regarding summary judgment from the Courts of Appeal. "The proper function of summary judgment is to terminate litigation when, as a matter of law, it appears that it would be impossible for the respondent to produce evidence at the trial warranting a judgment in his favor." *Smith v. Snow*, 106 S.W.3d 467, 468 (Ky. App. 2002), citing *Steelvest, Inc., v. Scansteel Service Center, Inc.*, 807 S.W.2d 476, 480 (Ky. 1991).[14]

**D. Alternatively, The Regulations Exceed The Scope Of The Enabling Statute And Conflict With Chapter 528 Prohibiting Gambling And Gambling Devices.**

As early as 1909, the courts recognized that along with the good associated with the magnificence of thoroughbred horse racing, there was an unfortunate aspect of "moral

[14]The Appellants' emphasis on *Manus, Inc., v. Terry Maxedon Hauling, Inc.*, 191 S.W.3d 4 (Ky. App. 2004) and *Goodyear Tire and Rubber Company v. Thompson*, 11 S.W.3 575 (Ky. 2000) is misplaced. in *Manus*, discovery had been conducted: "The admission in the Answer to the complaint as well as the deemed admissions eliminated any factual issues . . . " *Manus*, at 10. *Goodyear Tire* was whether a witness qualified as an expert witness under *Daubert v. Merrell Dow* case. It has no application here.

laxity", "temptation to fraud"", "scandals" and other conditions "inimical to public welfare" associated with wagering. *State Commission v. Latonia Agri. Ass'n*, 123 S.W. 681, 684 (Ky. 1909). "Any amusement which calls together vast throngs of people, which excites them in passion, or conduces to excesses, which is nearly always attended with gambling, and attracts among its patrons common gamblers, and the idle and vicious members of society, may be prohibited." *Id.*, at 685. Only times change . . . the nature of mankind does not. The General Assembly also recognizes the good in horse racing, but because of the bad there is also reason to scrutinize actions which may be harmful to the industry or to the public welfare in general. To this end, an exception to the broad prohibition of gambling in Chapter 528 was created by KRS 436.480 for "pari-mutuel wagering authorized under the provisions of KRS Chapter 230." The scope of the Commission's authority is not plenary. Instead, KRS 230.215(2) and KRS 230.361 vest the Commission with power to promulgate regulations under which pari-mutuel wagering is conducted on legitimate horse racing. All other wagering, gaming and even pari-mutuel wagering is outside the Commission's authority. If the Commission's statutory authorization is not expressed in Chapter 230, it is not excepted from Chapter 528 and thus does not exist. The Commission's statutory authority must be more carefully analyzed than most because its statutory authority is an exception from that which is otherwise prohibited. This question was addressed by the court in *Hargett v. Kentucky State Fair Board*, 216 S.W.2d 912, 917 (Ky. 1949), stating: "Careful scrutiny is always given to an exception to a general statute, and especially is this true when there is an exception permitting the carrying on of an activity generally declared to be against public

policy." In other words, while an agency may be entitled to deference in some situations, it is not.

The Appellants' reliance on *Public Service Commission v. Commonwealth,* 324 S.W.3d 373, 376 (Ky. 2010), and *Commonwealth v. Kentucky Public Service Commission*, 243 S.W.3d 374, 380 (Ky. App. 2007), is thus inapposite. In both cases, the Public Service Commission's authority was not derived from an exception to that which was otherwise prohibited. When authority is derived from an exception, careful scrutiny applies instead of deference. Here, the Appellants' admission that the Commission must have deference if it is to have authority is dispositive of the fact that authority does not exist.[15] Careful scrutiny demands that the Appellants carry the burden to make it perfectly clear that the Regulations are within the Commission's by alleging all the facts upon which their legal question depended. The Appellants failed in both of these regards. Ambiguity and/or secrecy is insufficient because not only are the Appellants required to allege all facts, "Any doubts concerning the existence or extent of an administrative agency's power should be resolved against the agency." *United Sign, LTD v. Commonwealth, Transportation Cabinet, Department of Highways*, 44 S.W.3d 794, 798 (Ky. Ap. 2000), citing *Flying J. Travel Plaza v. Commonwealth, Transportation Cabinet, Department of Highways*, 928 S.W.2d 344, 347 (Ky. 1996).[16]

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[15]Any other outcome violates the nondelegation doctrine embodied in the Ky. Constitution in §§ 27, 28, 29, and 60 as explained in *Board of Trustees of the Judicial Form Retirement Systems v. Attorney General*, 132 S.W.3d 770, 782-783 (Ky. 2003), *re'hg denied* (Ky. 2004).

[16]By analogy, *Revenue Cabinet v. Gaba*, 885 S.W.2d 706, 708 (Ky. App. 1994), which is cited by the Appellants, supports this requirement: "*General* tax statutes are to be construed in favor of the taxpayers, in cases of *statutory exemptions* from taxation, the converse is true." [Emphasis added].

Under KRS 13A.120, KRS 13A.140 and *Legislative Research Commission v. Brown*, 664 S.W.2d, 907, 919-920 (Ky. 1984), and other authority, the Commission may not promulgate regulations outside the scope of its statutorily delegated authority nor may it change a statute by regulation. The "regulations that would institute this product" are outside the Commission's authority. The Franklin Circuit Court erroneously referred only to KRS 230.215(2) and focused exclusively on the words "plenary power". Because "wagering" in KRS 230.215(2) is broader than the exception allowed by KRS 436.480, which is limited to "pari-mutuel wagering" only, KRS 230.215(2) is not determinative of the Commission's authority. But even if it was, the so-called plenary power is qualified to that which pertains to "legitimate horse racing and wagering thereon". KRS 230.361(1) is the applicable statute and limits the authority of the Commission to "governing and regulating mutuel wagering on horse races under what is known as the pari-mutuel system of wagering."

Even though KRS 230.215(2) is broader than the exception KRS 436.480 allows and KRS 230.361(1) appears in the preamble as one of the authorizing statutes, neither the Franklin Circuit Court nor the Dissent in the Court of Appeals even mentioned KRS 230.361(1). Assuming KRS 230.215(2) has some application, reading KRS 230.215(2) with KRS 230.361(1), the Commission's statutory authority is limited to (i) "pari-mutuel system of wagering", (ii) on "horse races", (iii) which are "legitimate horse racing and wagering thereon." Just as KRS 230.215(2) should not be ignored, the language limiting the "plenary power" in that statute likewise cannot be ignored. "[T]he reviewing court must attempt to construe the statue in such a manner that 'no part of it is meaningless or

ineffectual.'" *Combs v. Hubb Coal Corporation*, 934 S.W.2d 250, 252 (Ky. (1996), citing *Brooks v. Meyers*, 279 S.W.2d 764, 766 (Ky. 1955).

The Appellants have the cart before the horse. Contrary to the statutory and common law prohibitions, the Appellants purport to define "pari-mutuel wagering" in the Regulations. The Commission cannot make legal by subordinate regulations that which is illegal by statute. "Regulations are valid only as subordinate rules when found to be within the framework of the policy defined by the legislation." *Flying J Travel Plaza v. Commonwealth of Kentucky, Transportation Cabinet*, 928 S.W.2d 344, 347 (Ky. 1996). "A rule which is broader than the statute empowering the making of rules cannot be sustained. Administrative authorities must strictly adhere to the standards, policies, and limitations provided in the statutes vesting power in them. Regulations are valid only as subordinate rules and when found to be within the framework of the policy which the legislature has sufficiently defined." *Henry v. Parrish*, 211 S.W.2d 418, 422 (Ky. App. 1948). "[S]uch regulations are valid only when found to be within the framework of the policy defined by the legislation." *Whiteco v. Commonwealth of Kentucky, Transportation Cabinet, Department of Highways*, 14 S.W.3d 24, 27 (Ky. App. 2000), citing *Flying J. Travel, supra*. If outside the policy framework embodied by statute, such actions are outside the delegated power of the agency.

In *Legislative Research Commission v. Brown, supra*, the Kentucky Supreme Court visited the required separation of powers among the three branches of government. Until that time, the General Assembly had reserved to its interim committees the power to determine if regulations adopted by executive branch agencies comported with the statues which authorized them. This afforded the General Assembly near veto power over

regulatory actions of the executive branch. In *Legislative Research Commission v. Brown,* the Kentucky Supreme Court struck the power of the General Assembly holding that questions whether a regulation comported with the authorizing statute was a function of the judicial rather than the legislative branch. In so holding, the Supreme Court brilliantly reassured the General Assembly that there would still be a check on the power of the executive branch stating:

> There is no constitutional authority, however, whereby the governor can add, directly or indirectly, to the content of a statute by means of an administrative regulation and, a *fortiori*, no administrative regulation can be adopted unless it is necessary and is related to the content of the legislative act and to its effective administration.

*Id.*, at 919-920. The Kentucky Supreme Court told the General Assembly not to worry because it would not let the executive branch indirectly expand or nullify statutes by regulation. This Court's reassurance that it would limit the executive branch is now being put to the test by this appeal. To date, this Court has honored that promise by acknowledging that the plain words in statutes have meaning and are binding. In both *Commonwealth v. Fridge*, 962 S.W.2d 864 (Ky. 1998), and *Beckham v. Board of Education*, 873 S.W.2d 575, 577 (Ky. 1994), this Court held that courts are not at liberty to add to or subtract from a legislative enactment. In *Combs v. Hubb Coal Corporation*, 934 S.W.2d 250, 252 (Ky. (1996), this Court held that "[T]he reviewing court must attempt to construe the statue in such a manner that 'no part of it is meaningless or ineffectual.'" In *Commonwealth Transportation Cabinet, Bureau of Highways v. Roof*, 913 S.W.2d 322, 326 (Ky. 1996), this Court held that "A court is bound by the words chosen by the General Assembly." In *Musselman v. Commonwealth*, 705 S.W.2d 476, 478 (Ky. 1986), this Court said that "The statute must be tested on the basis of what is

said rather than what might have been said." *See also*, *Estes v. Commonwealth*, 952 S.W.2d 701, 703 (Ky. 1997). Consistent with *Legislative Research Commission v. Brown*, it was again stated: "[I]t is neither the duty nor the prerogative of the judiciary to breathe into the state that which the Legislature has not put there." *Wilson v. SKW Alloys, Inc.*, 893 S.W.2d 800, 802 (Ky. App. 1995). Similarly, this Court has warned that courts "may not interpret a statute at variance with its stated language." *Layne v. Newbert*, 841 S.W.2d 181, 183 (Ky. 1992). All this means that no court may ignore or jump over the words "legitimate horse racing", "mutuel wagering on horse races" and "pari-mutuel system of wagering" in KRS 230.215(2) and 230.361(1) when ascertaining the scope of the Commission's regulatory authority.

### 1. The Patented Instant Racing Product Is Not Pari-Mutuel Wagering And Does Not Involve Wagering Among, With or Against Each Other.

The essence of pari-mutuel wagering is wagerers wagering among themselves on a given event or defined group of future events. In *Commonwealth v. Kentucky Jockey Club*, 238 Ky. 739, 38 S.W.2d 987, 991 (Ky. 1931), Kentucky's highest court stated: "In French pools the operator of the game, which is played by use of a certain machine, the effect of which is that all who buy pools on a given race **bet as among themselves . . .** " [Emphasis in original]. The Interstate Horse Racing Act, 11 U.S.C. § 3002(13), cited by the Appellants, defines pari-mutuel wagering as requiring wagering "**with or against each other**". The Dissent in the Court of Appeals cited to *Let's Not "Spit the Bit" in Defense of "The Law of the Horse": The Historical and Legal Development of American Thoroughbred Racing*, 14 Marq. Sports L. Review, 473, 496 (2004), by Joan S. Howland, who stated: "Critical to the legality of the system is that the bettors wager **among**

**themselves** rather than against the operator of the pool (i.e., the Racing Associations or the 'house')." [Emphasis in original]. Similarly, *Horse Race Betting; A Comprehensive Account of Bookmaking Operations 3* (1946), Frank Buck explained pari-mutuel wagering as: "The term 'pari-mutuel' as a contraction combining the French verb 'parier,' meaning 'to wager,' and the French word **'mutuel,' which may be translated as 'between ourselves.'"** [Emphasis added]. Commission, Memorandum in Support of Petition for Declaratory Judgment, p. 11. R. III, 11, The Appellants have cited no authority in which true pari-mutuel wagering does not require wagerers to be betting among, with or against themselves.[17]

The Appellants do not disclose the fact that under the Regulations, the Commission granted itself the authority to approve wagering in which there is absolutely no pooling of wagers among wagerers competing on the same event or group of events. Because the patented instant racing gaming scheme involves only a "trivial pool of one" arising from a wager on a "unique event" as opposed to wagerers wagering against themselves on a single event or single group of events, pari-mutuel and wagering pool were incapable of being limited by the Regulations and still empower the Commission to institute the patented instant racing product which would be excepted from application of Chapter 528 by KRS 436.480 of the Kentucky Revised Statutes. The Appellants did not disclose the fact that the instant racing patent by its terms is not pari-mutuel wagering even though they were required to do so under KRS 418.020. Regardless, the instant

[17] Self serving opinions of associations form no basis for whether instant racing is or is not pari-mutuel and should be disregarded in this case. If nothing else, however, those factual assertions by the Appellants confirm the need for discovery so those assertions can be cross-examined.

racing product is not pari-mutuel wagering under the definitions of pari-mutuel wagering above. The instant racing patent no. 6,358,150 describes the gaming scheme as:

> The present invention emphasizes the role of the progressive carry-over pools, so that all tiers of winning payoffs are made from progressive pools. Each player is presented with a **unique event**, **so there is no pooling of other players' wagers on that event**. **Each wager forms a trivial pool of one, and either loses and is apportioned among the tiers of progressive pools, or wins and is awarded one of the progressive pools. Since the event is served up on demand from the historical library, not on a schedule, a winning payoff may be made instantly.** [Emphasis added].

FF Br. 19-20, Exhibit H, R. V. The instant racing patent explains a system by which the patron bets on a "unique event" in a "trivial pool of one". That trivial pool of one is then collated from all sources into subsequent non-mutuel progressive pools. "[T]here is no pooling of other players' wagers" on the same event. The Instant Racing Patent summarizes the instant racing product on p. 9 as follows:

> In pari-mutuel wagering, the players are playing against each other, and the 'house' or the establishment conducting the game receives a commission on all wagers placed. Parimutuel wagering games are distinguishable from slot games or non-parimutuel wagering games where the players are playing against the 'house' or establishment conducting the game. The gaming [sic] system in one embodiment includes a plurality of terminals coupled to a game server through, for example, a wide area network such as the internet. The terminals are computers communicably connected to a wide area network and include a user interface such as a keyboard and a video monitor. The terminals enable a player to establish an account, to enter a wager, to receive a video-audio play-back, and to review the player's account balance. The game server is a computer system configured to manage the entire game system. For example, the server maintains databases, maintains player accounts, controls and accounts for the transactions with the terminals, controls the flow of data from a video server to the terminals, **collates pools from all sources** and computes winnings, and provides detailed statistics for the disbursement of funds. The gaming system also includes a video server interface for providing delivery of selected video images from a historical database. [Emphasis added].

The Appellants do not disclose the fact that bets from patrons of instant racing are collated by a server. Regardless, a wagerer plays the instant racing game at a terminal which is connected to a server which manages the game and "collates pools from all sources". A collation of pools from all sources is the antithesis of pari-mutuel wagering pools. The collated pools are a collection of lost wagers over a period of time spanning hundreds and thousands of videos of previously run horse races. Absent from all of the Appellants' briefs is any explanation as to how the function of this collation of pools equates to pari-mutuel pools where wagerers are betting with, among and against one another. The Appellants' analogy to Pick Six or the Daily Double games is inapplicable because those games are defined events on which odds can be calculated, not 22,000 random potential combinations of videos upon which bets may be place over a period of years upon which odds cannot be calculated.

The lower court confused (i) the collation trivial pools of one -- into progressive pools, in which no wagerer has bet, with (ii) pari-mutuel wagering pools into which patrons betting against each other have placed their bets.[18] Collating pools of individual bets does not convert slot machine betting into pari-mutuel wagering. Of course, discovery would have revealed this fact and permitted an evidentiary record which would have avoided the misunderstandings of the Franklin Circuit Court and the Dissent in the Court of Appeals.

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[18]The Dissent in the Court of Appeals referred to 810 KAR 1:001(48) which defines "pari-mutuel wagering" as a scheme where "patrons are wagering against themselves . . ." Then after correctly recognizing the requirement that a wagering pool be composed of wagerers who are betting against themselves, the Dissent correctly acknowledged that with instant racing "the participants bet on different races". The concepts are mutually exclusive.

With regard to the definition of pari-mutuel wagering, the Appellants do not disclose additional facts that the Commission has granted itself the power to approve as pari-mutuel wagering those wagers which are not in the same pool. This is a material fact upon which the Appellants' question depends which was not disclosed. Obviously, the Appellants could not declare this fact, because it is to be subsequently determined by the Commission: as "a system or method of wagering *approved by the commission* in which patrons are wagering among themselves and not against the association and *amounts wagered are placed in one or more designated wagering pools* and the net pool is returned to the winning patrons." 801 KAR Section 1, 1:001(49); 811 KAR Section 1, 1:005(67), and 811 KAR Section 1, 2:010(59). Critical here is that under the proposed system of wagering and Regulations, the wagers do not have to be placed in the same wagering pool. This fact is dispositive of the Appellants' legal question because this means that the Commission may approve, and has approved, systems and methods of wagering which are not pari-mutuel under the definitions of pari-mutuel.

The Regulations were cleverly drafted (i) to falsely declare as fact that all wagering on historical horse racing is authorized,[19] (ii) to falsely declare as fact that all wagers on historical horse races are exotic wagers,[20] (iii) to falsely define any exotic

[19] The Regulations declare that: "Wagering on an historical horse race is hereby authorized and may be conducted in accordance with KRS 230 and these administrative regulations." 810 KAR 1:011, Section 3; 811 KAR 1:125, Section 3; and 811 KAR 2:060, Section 3.

[20] The Regulations declare that "Any wager placed on an historical horse race is an exotic wager." 810 KAR 1:011, Section 3(5); 811 KAR 1:125, Section 3(5); and 811 KAR 2:060, Section 3(5).

wager as any pari-mutuel wager on a historical horse race,[21] and (iv) to falsely define pari-mutuel wagers as that which is determined by the Commission to be pari-mutuel wagering, even if deposited into separate undefined pools - which are not pools.[22] Then *voila,* by regulatory fiat, the Commission purported to converted an illegal patented gaming scheme into legal pari-mutuel wagering on legitimate horse racing by regulations authorizing the Commission to find something is what it is not. They even purport to bring dead horses back to life. No wonder the Appellants insist that all discovery be barred.

The Regulations which define "Pari-Mutuel Wagering" provide that pari-mutuel wagering is a system or method of wagering approved by the Commission" in which "amounts wagered are *placed in one or more designated wagering pools.*" [Emphasis added]. Nowhere in the definition is the Commission limited to approving pari-mutuel wagering in which amounts are placed in the same wagering pool. A gaming scheme in which wagers are not placed in the same wagering pool is not pari-mutuel wagering under the definitions of pari-mutuel wagering above. Important to note is that "wagering pools" is not defined in the Regulations, leaving the Commission free to define it as something it is not -- which it has done its first three instant racing approvals. No where

[21] The Regulations define "exotic wager" as "any pari-mutuel wager placed on a live or historical horse race other than a win, place, or show wager placed on a live horse race." 810 KAR 1:001, Section 1(27); 811 KAR 1:005, Section 1(37), and 811 KAR 2:010, Section 1(32).

[22] The Regulations define "Pari-mutuel wagering" " as "a system or method of wagering approved by the commission in which patrons are wagering among themselves and not against the association and amounts wagered are placed in one or more designated wagering pools and the net pool is returned to the winning patrons." 801 KAR Section 1, 1:001(49); 811 KAR Section 1, 1:005(67), and 811 KAR Section 1, 2:010(59).

do the Regulations require wagers from wagerers who are wagering with/against one another be pooled. That is another fact upon which the Appellants agreed case depended which they did not disclose.

### 2. Videos Of Previously Run Horse Races Are Videos -- Not Horse Races.

KRS 230.215(2) and KRS 230.361(1) limits the Commission's authority to horse races. Words of the statute must be given their plain meaning. "Where there is no specific statutory definition, we must construe the words of the statute within their common usage." *Alliant Health System v. Kentucky Unemployment Insurance Commission*, 912 S.W.2d 452, 454 (Ky. App. 1995). In this respect, horse races and horse racing does not mean videos -- which is why the Kentucky Attorney General excepted devices from his 2010 opinion. The words "wagering on horse races" means exactly what they say. The common usage of horse races is the event in which horses are competitively raced against one another. The statute does not say "wagering on a video of a previously run horse race." Such an alteration of the plain meaning of the words actually used is not within the common usage of the words and is not a permissible construction of the statute. As such, the Commission is empowered to promulgate wagering on horse races, not videos on gaming devices.

### 3. The Appellants Do Not Describe How A Video Is A Legitimate Horse Race.

Since a horse race cannot be replicated by a video, movie or digital game, the analysis is not complicated. To be within the Commission's statutory authority, the subject matter of the Regulations must be "legitimate horse racing" not videos or reels. If the gaming scheme is not based on actual "horse racing", then it is not within the

statutory jurisdiction of the Commission. Clearly, KRS 230.215(2) and KRS 230.361(1) does not empower the Commission to authorize betting on videos of previous horse races displayed on a reel device any more than it authorizes betting on greyhound racing, jai-alai, videos, movies, films, slide shows or YouTube. The only exception from the prohibition of illicit gambling is pari-mutuel wagering on legitimate horse racing. KRS 436.480. Because instant racing is a game where patrons bet on videos, not actual horse races, the scheme is not horse racing and is outside the scope of the Commission's authority.

According to 810 KAR 1:010, Section 1(7)(d) of the Regulations: "Prior to the patron making his or her wager selections, the terminal shall not display any information that would allow the patron to identify the historical race on which he or she is wagering, including the location of the race the date on which the race was run, the names of the horses in the race, or the names of the jockeys that rode the horses in the race." 810 KAR 1:010, Section 1(7)(f) of the Regulations provides that "After a patron finalizes his or her wager selections, the terminal shall display a video replay of the race, or a portion thereof, and the official results of the race. The identity of the race shall be revealed to the patron after the patron has placed his or her wager."

Under this description the names of the horses in the races are concealed until after a patron finalizes his or her wager selections. This was the same material observation about instant racing made by the Maryland Attorney General. "Before making a selection, the player has the opportunity to examine past performance data, originally published on the day the race was held, showing the records of the entries at the time. [Citation omitted]. However, information identifying the race, the race track,

the horses participating in the race, and the owners, trainers and jockeys of those horses is withheld until after a wager has been made." The information identifying the race, the race track and the horses is withheld. Assuming for purposes of argument that wagering on a video of a previously run horse race is a "horse race" within the meaning of KRS 230.215(2) and KRS 230.361 and is "live racing" within the meaning of KRS 138.510(1)(a), it is still not permitted under Chapter 230 because it is not a legitimate horse race.

The Appellants emphasize that a video no different than a live horse race. If an instant racing video is the same as a horse race, then not even in the Commission's and the Department's virtual world is it permitted because under Kentucky law a horse's name may not be concealed, assumed or changed.

KRS 230.070 provides that:

> No person shall knowingly enter or cause to be entered for competition, or compete, for a prize or stake, or drive any horse, under an assumed name, or out of its proper class, where the prize or stake is to be decided by a contest of speed.

KRS 230.080 provides that:

> No person shall change the name of any horse for the purpose of entry for competition in any contest of speed, after the horse has once contested for a prize or stake, except as provided by the code of rules of the association under which the contest is advertised to be conducted.

The Appellants do not disclose the fact that concealment of the *virtual* horse's identity is essential if patrons are going to bet on the video without knowing the outcome of the virtual race as contemplated by the Regulations. If the name of the horse may not be concealed in actual horse racing, it may not be concealed in the Appellants' virtal horse racing on videos. If the name and other handicapping information is concealed, the horse

racing is not "legitimate". It is a "charade". If the Commission wants to pretend that past horse races are the same as present horse races then the same rules must apply to both. The Appellants resurrect a 1960's hyper-reality theme, arguing that the medium is the message.[23] Race Tracks Brief at 27. They argue that a 2" x 2" three second display of a video on the top right corner of a slot machine display (the medium) is a horse race (the message). Under their new virtual reality standard, the past is the present, the present is the future, the dead is living and the imagined is real. In the Appellants' land of fiction, continuums of time, space, logic and moreover common sense no longer exist.

Along with their virtual reality theme, the Appellants argue that because the word "live" does not appeal in KRS 230.215(2) or in KRS 230.361(1), that "horse races" and "horse racing" includes video games. The silliness of the Appellants arguments is demonstrated by the following simple illustration. According to them, a wagerer who bets alone on a reel device which happens to display a 2" x 2" three second video of the end of the Seabiscuit – War Admiral match-up in 1938 at the Pimlico Race Course, is engaged in pari-mutuel wagering on legitimate horse races. Even though (i) the race occurred 75 years ago and Seabiscuit died in 1947 and War Admiral in 1959, (ii) the race is a 2" x 2" video and not a horse race, (iii) the year of the races, the owners, the trainers and the jockeys are concealed, (iv) the race occurred in the past and both horses are dead, (v) at no time are two or more wagerers are betting against each other, and (vi) the odds/chances of winning are pre-determined by the host, the Appellants say this is pari-mutuel wagering on legitimate horse racing. To state the obvious, in order for the this

[23]McLuhan, Marshall, "Understanding Media; The Extensions of Man" Mentor, New York (1960).

video gaming scheme to be pari-mutuel wagering on legitimate horse racing, false premises must be assumed as true. History must occur in the future. A video has to be a present reality. Alive must includes the dead. Patrons betting on different videos, in different years, at different locations must be betting against each other at the same time on legitimate horse racing. A pool of one has to be the same as a pool of many. Patrons who bet on separate events must be deemed to be betting against each other on the same event. Singular progressive pools with no competing wagerers must be the same as a mutuel pool of competing wagers. Only in a land of pretend facts does the Commission's and the Department's authority extend to such a gaming scheme.

### E. The Department Purports To Adopt A Purely Subjective Standard.

The Kentucky Department purported to amend its Form 73A100 upon which wagering and excise taxes are paid, to include reporting and excise taxes on wagering on videos of previously run horse races. On August 12, 2010, the Department adopted draft regulations to amend 103 KAR 3:050, the Miscellaneous Taxes Forms Regulations which incorporates the modification to Form 73A100, to provide:

> Racing Taxes – Required Form. Revenue 73A.100, "Race Track Pari-Mutuel and Admissions Report", shall be used by race tracks licensed by the Kentucky Horse Commission to report liability for the pari-mutuel tax and to report admissions to the race track.

KRS 138.510(1)(a) limits excise taxes which may be collected to those from wagering on "live races". As pointed out above, courts must give meaning to all the words in a statute. "[T]he reviewing court must attempt to construe the statue in such a manner that 'no part of it is meaningless or ineffectual.'" *Combs v. Hubb Coal Corporation*, 934 S.W.2d 250,

252 (Ky. (1996). The Court may not ignore the words "live racing" within KRS 138.510(1)(a). So, the Department relies on the statutory definition of "daily average live handle" in KRS 138.511(3). The Appellants and the Department did not ask for a declaration in the joint petition that KRS 138.511(3) allowed an excise tax. Instead, the Department was very specific in its request for an advisory opinion whether it had authority to tax betting on videos under KRS 138.510(1).

The Department argues that "From the perspective of a wagerer, a historic horse race if very much 'live' -- the wagerer does not know the outcome of the historical horse race in advance of wagering on the race any more than a wagerer at a track knows the outcome of a race physically conducted at that track." Department Brief at p. 8. In other words, the Department seeks to determine whether it can assess excise taxes based on the subjective understanding of a wagerer who cannot tell that he is betting on a video on a gambling device that took place 20 years ago instead of on a live horse race with real animals which is happening before his eyes.[24]

**F. Agency Deference Is Impermissible When Agencies Admit That They Do Not Know If Their Actions Are Legal.**

"*Res ipsa loquitur*" – the thing speaks for itself – belies the Appellants' claim of agency deference. Agency deference stems from a belief that an agency possesses a particular technical or historical expertise, neither of which are present here. The Commission and the Department filed the joint petition because they admittedly did not know if the Regulations and their implementation were legal. It is duplicitous for the

[24]The pressure on the Department of Revenue from the Finance Cabinet, the Secretary of which is married to the vice-president of appellant, Churchill Downs, Incorporated, must have been extraordinary to require such arguments.

Appellants to demand deference to answers to questions to which they admit by filing this case that they do not know the answer.

In *Mid-America Care Foundation v. National Labor Relations Board*, 148 F.3d 638, 642 (6th Cir. 1998), which also explained the limited application of *Chevron USA, Inc. v. Natural Resources Defense Council*, 467 U.S. 837, 104 S.Ct. 2778, 81 L.Ed.2d 694 (1984):

> ]B]oth the Supreme Court and our court have made clear that there are numerous instances in which an agency's interpretation of an ambiguous state is not entitled to the broad deference envisioned by *Chevron*. **An agency's interpretation is not entitled to *Chevron* deference, for example, if the apparent statutory ambiguity can be resolved using 'traditional tools of statutory construction.'** [citation omitted]. Similarly, courts do not accord *Chevron* deference to non-binding advisory opinions of an administrative agency. [citation omitted]. **Nor does *Chevron* deference extend to an interpretation taken solely in connection with an agency's litigating position in a particular case or set of cases.** [citation omitted]. . . . However, as the Supreme Court explained just this year, when an agency's application of a statutory interpretation (which itself ordinarily would be entitled to deference) frustrates judicial review by 'subtly and obliquely' revising the stated interpretation to impose a more stringent definition or a higher standard of compliance in certain factual contexts, *Chevron* deference is inappropriate. [citation omitted]. [Emphasis added].

*Mid-America*, at p. 642. KRS 230.215(2), KRS 230.361 and KRS 138.510 can be interpreted with the use of well recognized tools of statutory construction. Further, the Commission and the Department are in litigation. Both chose to institute litigation in cooperation with the Race Tracks. To afford executive branch agencies the benefit of interpretation of their enabling statutes should strike an offensive cord to the judiciary which has decades of precedent as to how it interprets statutes.

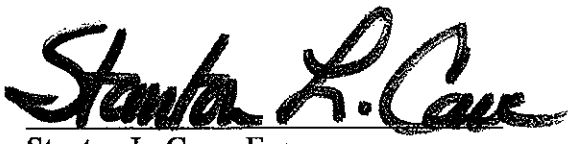
*Homestead Nursing Home v. Parker*, 86 S.W.3d, 424, 426 (Ky. App. 1999), must be interpreted in the context of *Western Baptist Hospital v. Kelly*, 827 S.W.2d 685, 687-88 (Ky. 1992), where the Kentucky Supreme Court held: "The [Workers Compensation Board] is entitled to the same deference for its appellate decisions as we intend when we exercise discretionary review of the Court of Appeals decisions that originate in circuit court. The function of further review of the WCB in the Court of Appeals is to correct the Board only where the [ ] Court perceives the Board had overlooked or misconstrued controlling statutes or precedent, or committed an error in assessing the evidence so flagrant as to cause injustice." In other words, the reviewing court has unrestricted power to correct an error of an agency if the agency has committed an error. The *Homestead Nursing Home* court even recited this language in its opinion at p. 426. The Appellants' argument that this Court is to abandon well recognized rules of statutory construction to agencies who choose to ignore their own authorizing statutes would turn constitutionally required separation of powers on its head.

## VI. CONCLUSION

The Family Foundation was entitled to conduct discovery to obtain information and facts upon which the Appellants' legal question depended requiring the Court of Appeals to be affirmed; or the Appellants failed to set forth all the facts upon which their legal question depended and their joint petition must be denied requiring the Franklin Circuit Court to be reversed. No other outcomes are supported by law. The Family Foundation respectfully requests that the Court of Appeals be affirmed, that the Opinion and Order of the Franklin Circuit Court, entered December 29, 2010, be vacated, that The Family Foundation be allowed to conduct pretrial discovery and that this case be

remanded back to the Franklin Circuit Court for further proceedings; or, in the alternative, that the Franklin Circuit Court be reversed and that the Appellants' joint petition be dismissed for failing to allege and disclose all the facts upon which the Appellants' question depended.

Respectfully submitted,



Stanton L. Cave, Esq.
LAW OFFICE OF STAN CAVE
*Counsel for the Appellee, The Family Trust Foundation of Kentucky, Inc., d/b/a The Family Foundation*

## APPENDIX

| DESCRIPTION | EXHIBIT |
| --- | --- |
| Court of Appeals Opinion Vacating and Remanding, June 15, 2012, | A |
| Franklin Circuit Court Memorandum Opinion and Order December 29, 2010 | B |
| Franklin Circuit Court, Order Denying Discovery, September 23, 2010, | C |
| Transcript, September 20, 2010 hearing, page 8 | D |
| Transcript, September 20, 2010 hearing, page 4 | E |
| Transcript, December 14, 2010 hearing, page 43 | F |