

**CALIFORNIA GAMBLING CONTROL COMMISSION**

**INITIAL STATEMENT OF REASONS**

**CGCC-GCA-2008-R-3**

**HEARING DATE:**

November 18, 2008

**SUBJECT MATTER OF  
PROPOSED REGULATIONS:**

Minimum Internal Control Standards (MICS) for Gambling Establishments: General Terms, Conditions & Definitions; Policies & Procedures; Drop & Drop Collection; Count & Count Room Functions; and Cage Functions.

**SECTIONS AFFECTED:**

**California Code of Regulations, Title 4, Division 18, Chapter 7, Article 3, Adopt Sections 12380, 12381, 12384, 12385 and 12386.**

**SPECIFIC PURPOSE OF REGULATORY PROPOSAL:**

**Introduction:**

The California Gambling Control Commission (Commission) is the state agency charged with the administration and implementation of the California Gambling Control Act (Act).<sup>1</sup> The Commission is authorized to adopt regulations governing the operation of gambling establishments (or “cardrooms”) in California.<sup>2</sup> Specifically, the Commission is mandated to adopt regulations on the subjects enumerated in Business and Professions Code,<sup>3</sup> section 19841. Regulations concerning the establishment of minimum policies and procedures by owner licensees to exercise effective control over their internal fiscal and gambling affairs have been prepared in compliance with section 19840<sup>4</sup> and subdivisions (h) and (i) of section 19841.<sup>5</sup>

Gambling is the quintessential cash business and internal controls are the primary procedures used to protect the integrity of cardroom funds and games. Internal controls are therefore a

---

<sup>1</sup> Business and Professions Code, Division 8, Chapter 4, § 19800 et seq.

<sup>2</sup> See Business and Professions Code § 19840.

<sup>3</sup> All statutory references are to the Business and Professions Code, unless otherwise specified.

<sup>4</sup> § 19840 provides, in pertinent part, that “[t]o the extent appropriate, regulations of the Commission ... shall take into consideration the operational differences of large and small establishments.”

<sup>5</sup> Subdivision (h) of § 19841 mandates that the Commission’s regulations shall “[p]rescribe minimum procedures for adoption by owner licensees to exercise effective control over their internal fiscal and gambling affairs,” as specified. Subdivision (i) mandates that the Commission’s regulations shall “[p]rovide for the adoption and use of internal audits, whether by qualified internal auditors or by certified public accountants” as a means of “testing and evaluation of other controls” for the purpose of “observing proper compliance with the minimum standards of control prescribed in subdivision (h).”

vitality important part of properly regulated gambling. In general, the proposed action has been drafted in an attempt to establish uniform procedures and standards to assist the Commission and the Bureau of Gambling Control within the Department of Justice (Bureau) in meeting their oversight responsibilities under the Act, while taking into account the variations in size of gaming operations. Perhaps more importantly, the proposed action is intended to assist cardrooms in safeguarding their assets, protecting patrons and their property, and maintaining the integrity of games and gaming. These regulations establish a baseline for cardroom operation, by requiring that licensees establish and implement written policies and procedures that meet or exceed the prescribed MICS, as they relate to the established size category of the individual licensee. Establishing a baseline standard helps to ensure consistency and uniformity.

**Background:**

The Commission's involvement in the development of MICS for gambling establishments began in June 2004. A joint Commission-Bureau-Industry workshop was conducted to review preliminary draft proposals for regulations in September 2004. After consideration of the information and comments received through that workshop, the proposed MICS requirements were given to the Bureau's auditors who were to assess the feasibility of some of the requirements in relation to the auditors' actual experiences in the field. Instead of one large rulemaking with many MICS included, the decision to have smaller rulemaking packages with topic-related MICS was made. The regulations on Gaming Activity and Additional Tables requests finished the rulemaking process in 2006, with the latter being adopted and approved. Subsequently, other issues arose which required the Commission to re-evaluate their regulation development priorities and work on the MICS regulations was suspended temporarily.

In September 2007, a joint Commission/Bureau MICS Regulations Workgroup was formed to continue the development of regulations to establish MICS for cardrooms. The workgroup has discussed general MICS requirements and researched MICS requirements from other states. Due to the number of subjects and complexity of the MICS requirements, the workgroup segregated the requirements into separate subject areas in order to pursue regulations in phases according to priority. Those subjects and phases, in order of priority, are:

**Phase**

- I. General Terms, Conditions & Definitions; Policies & Procedures; Drop & Drop Collection; Count & Count Room Functions; and Cage Functions
- II. Security & Surveillance
- III. Gambling Floor Operations & Play of Table Games
- IV. Chips, Cards & Other Gambling Equipment
- V. Personnel & Tips
- VI. Information Technology Systems
- VII. Adequate Financing; Players' & Dealers' Banks, and Jackpots

Multiple phases are being considered simultaneously and are currently in various stages of development. It is intended that each phase will be taken up, formally, in the order listed above. While this proposed action encompasses Phase I alone, both Phase II and Phase III are currently undergoing development as well.

MICS-related regulations on Check Cashing, Extension of Credit, and Abandoned Property have been taken up in a separate rulemaking proposal that was noticed earlier this year.

The workgroup completed an initial draft proposal for Phase I and scheduled an informal public comment session to solicit comments from the industry on the draft proposal. The informal public comment session was held December 11, 2007. All comments were recorded and categorized, and were considered in the further development and refinement of the Phase I proposal. A modified draft proposal was completed and distributed to interested parties in early March 2008, and additional written comments were solicited. Further revisions were made to accommodate many of the comments and suggestions received and this proposed action was formed. Additional public comments and recommendations were also accepted at the September 10, 2008 Commission meeting when the Commission approved the commencement of the formal APA rulemaking process. The September 10<sup>th</sup> comments will be included in the rulemaking file and considered along with any comments received during the 45-day comment period for this proposed action. A great deal of effort has been made to include affected parties in the development of this proposed action and careful consideration has been given to their views and suggestions, as well as the physical and economic differences between the various card rooms throughout the state.

**Proposed Action:**

This proposed action will make the following changes in Chapter 7 of Division 18 of Title 4 of the California Code of Regulations:

Article 3. will be amended to incorporate minimum internal control standards (MICS) for gambling establishments as follows:

1. Adopt Section 12380 which will define “minimum internal control standards” (MICS) for the purpose of Chapter 7, will establish the basic application of MICS in the operation of cardrooms and will make failure to comply with this article a ground for disciplinary action. This section will also establish five specific licensee “tiers” based on a licensee’s number of approved gaming tables, and will contain general definitions of terms used throughout Article 3 in relations to MICS.
  - This section, through subsections (a) and (b), provides the basic foundation for, and sets forth the general purpose of the MICS requirements. In that regard, this section is intended to be informative and a guide in interpreting and applying the specific standards and requirements that follow.
  - Subsection (c) is also intended to be informative and clarifying. Licensees are put on specific notice that failing to comply with the requirements of this article or to cure any deficiency, as specified in a determination issued by the Bureau, constitutes an unsuitable method of operation and is a ground for disciplinary action. It is important and proper that licensees be made aware or reminded of the possible consequences of their actions or inaction.

- The establishment of licensee tiers in subsection (d) is intended to be an uncomplicated, understandable and succinct means of distinguishing variations in the size of cardrooms. In the vast majority of instances, the number of approved gambling tables a cardroom is licensed to operate has a direct correlation to the size of the operation – both physical and fiscal. In order to be able to consider the “*the operational differences of large and small establishments*” in the construction and application of its regulations,<sup>6</sup> the Commission must have standards that are easy to interpret, and to apply as efficiently and fairly as possible. The number of tables has been determined to be a relatively consistent means of making these distinctions.
  - The definitions in subsections (e) and (f) of “Security Department” and “Surveillance Unit” provides a general description, for purposes of this article, of two terms that are used throughout the MICS regulations, including this proposed action – Phase I. Subsection (e) is intended to set out the general parameters of what a security department’s responsibilities might include or the functions that might be shared with another entity. The same is intended in subsection (f) with respect to a surveillance unit, as well as establishing the general requirement for staffing of such units. While ultimate responsibility for overall compliance with the Gambling Control Act rests with the owner licensee, certain units or departments are generally seen to cover certain aspects of the day-to-day operations of a cardroom. For instance, security is usually in the best position to keep an eye on the property of the cardroom and its patrons and employees. Both security and surveillance share in the first-line of defense against underage gambling.
2. Adopt Section 12381 to establish clear and consistent requirements for the establishment by licensees of minimum policies and procedures addressing each major element of operation of their gambling establishments. This section will require the establishment of policies and procedures for MICS, the communication of those policies and procedures to employees, adherence to the established policies and procedures, and the availability of those policies and procedures to the Commission and Bureau. Provisions are included for the Bureau to issue determinations regarding deficiencies and for timely curing those deficiencies. This section also includes basic requirements for record keeping. Finally, licensees in tiers II through V will be required to assign specified duties and responsibilities concerning policies and procedures to a designated member of management.
- Subsection (a) requires that policies and procedures be in written form. This is intended to ensure that there is a physical document that can be relied upon to determine, first of all, compliance with the requirement policies and procedures; and secondly, the adequacy of those policies. Having written policies and procedures also provides a reliable means of ensuring that all employees are made aware of their requirements and facilitates compliance with subsection (b).

---

<sup>6</sup> See Business and Professions Code § 19840.

- Requiring, in subsection (b), that the licensee's policies and procedures be communicated to its employees is intended to ensure that the employees are made aware of those requirements and any subsequent modifications. Properly informed employees will provide greater assurance that a higher level of compliance will be achieved and maintained. This will also assist licensees in complying with subsection (c).
- Subsection (c) simply requires adherence to the licensee's established policies and procedures. While requiring the establishment of policies and procedures might imply the adherence is mandated, it is not clear. Without this specific clarifying requirement, establishing policies and procedures could be meaningless.
- Subsection (d) establishes the Commission's and Bureau's basic right of access to licensees' policies and procedures. This access is necessary to facilitate a review by the Bureau in order to assess the adequacy of the policies and procedures so that a determination may be issued pursuant to subsection (e).
- Subsection (e) addresses those instances in which the Bureau, in its review of a licensee's policies and procedures, may find deficiencies. In the event that the Bureau determines that a licensee's established policies and procedures are not adequate, this provision establishes a basic procedure for the licensee to cure the deficiency. This is intended to inform licensees of what they may expect in these circumstances. The standards specified are intended to give both the Bureau and licensees flexibility in working out specific details and time frames for responses and corrective action.
- The establishment of minimum basic requirements for the maintenance of records is covered in subsection (f). Permanent records must be maintained to provide a basis for regulatory compliance review. As state agents and auditors will review the records, they shall be maintained in English, so that those individuals may read them. The minimum retention period of three years is adequate for several of the records addressed in this article, except those records for which a longer retention period may be required; for example, accounting and financial reporting records addressed in Article 4 of Chapter 7. Records must be available to the agents and/or auditors during the hours when the responsible cardroom management/employees would normally have access to the records – the night shift, for example, may not always have access to accounting documents when the staff of the accounting department has left for the evening.
- The requirements, in subsection (g), that licensees in Tiers II through V assign the responsibilities for establishing, reviewing, monitoring, and testing for compliance the MICS policies and procedures; that specified periodic testing be done; and that compliance test results be reported, implement the provisions of Business and Professions Code section 19841, subsections (h) and (i). These requirements are made applicable to only Tiers II through V, as Tier I licensees are generally so small, with management limited to an individual owner or a single employee, that

assignment or delegation of these requirements would be impractical, if not impossible. Furthermore, the general accounting and reporting requirements applicable to all licensees,<sup>7</sup> including Tier I licensees, are adequate for this purpose as the risk potential is relatively minimal.

3. Adopt Section 12384 to provide for the inclusion in a licensee's policies and procedures of standards to address the deposit of fees into a secure container and periodic collection of those containers. When patrons of a cardroom engage in controlled gambling, they pay a fee, either per hand or per hour, for playing. This fee – either in regular chips or nondenominational drop-chips – is “dropped” into a “drop box” attached to the gambling table, and the boxes are collected at certain times each day by the cardroom. This is the main source of cardroom revenue and must be both protected (if chips are used) and accurately reported. This section will provide specifications for the construction, use, and basic security of drop boxes. In addition, this section will establish the extent and complexity of these requirements as they apply to the licensee tiers established in Section 12380.

In general, the basic requirements governing drop boxes and drop collections serve not only to safeguard licensees' assets, but also to assist the Bureau in its regulatory role. There have been numerous instances where a Bureau cardroom audit/review has found that more drop boxes were being collected than the total number of tables authorized for that licensee. The identification and tracking of drop boxes and the scheduling of drop box collections could be important factors in confirming that a licensee has illegally operated more gambling tables than authorized under its license.

#### **All Tiers**

- Subsection (a), paragraph (1), requires the use of a secure container (drop box) for the collection of drop and other fees. The drop box must be secured to the gambling table and constructed and controlled so as to provide for the security of its contents. As most cardrooms place chips in the drop box, it is important that the box be secured so that unauthorized persons cannot take any chips out of the drop box.
- Paragraph (2) requires the use of a separate drop box or other method of segregation, and a separate accounting, for jackpot or similar collections. Jackpot collections have separate accounting requirements, thus the drop must be kept separate from any jackpot collections. The separation or segregation may be accomplished by the use of a second drop box or by some other means. For example, if drop chips are used exclusively for fees, but not for jackpots, segregation is still achieved even though a single drop box is utilized.
- Paragraph (3) establishes basic standards for the construction of drop boxes. In order to properly secure the drop box, separate locks close the box and attach it to the gambling table. The box needs to be clearly and visibly marked (with table numbers or letters, and shift identifiers – such as AM or PM, or symbols indicating time of day

---

<sup>7</sup> See Article 4, § 12400, et seq.

(e.g., sun, moon) – if more than one box per day is used) as to which table it should be attached. The box must also have an opening through which chips may be inserted.

Requiring separate locks to secure the contents of the box and to secure the box to the gambling table provide multiple levels of security. First, securing the box to the table protects against tampering, theft or unauthorized removal of the box itself. Second, a separately keyed lock securing the contents of the box provides a means of restricting access to the contents by unauthorized personnel (e.g., employees performing the drop box collection would have the keys to the locks securing boxes to tables but not to the locks securing the contents of boxes.)

The identification of drop boxes and the linking of the box to its corresponding table is an important element in a complete audit trail. Through this identification the drop boxes, when collected, can be followed from the table to and through the count. Visible identifiers can be tracked through surveillance video. As a supplement to visible identifiers, provision is also included for electronic identification using a bar code or similar system. In a bar code identification system, the box, the table, and the personnel collecting the boxes all have individual bar code identifiers. The system records those identifiers and all other relevant information for the drop collection. That information can then be accessed at a later time for comparison to the video recording of the collection.

While it may seem obvious that there must be an opening in a drop box to provide for the deposit of chips, this requirement is included for clarity and specifically requires that the chips collected for the drop and other fees actually be deposited into the box.

- Paragraph (4) permits the use of an emergency, interim or temporary drop box. Sometimes, cardrooms use a different box to collect the drop, either due to heavy usage necessitating that the box be changed out, or because the original box requires maintenance. In such instances, cardrooms use a box that they mark emergency, interim, or temporary, depending on the cardroom and/or reason for the switch. Extra boxes are kept on site for such times, but not as many extra boxes as tables are required. The use of such a temporary box does not require any permanent table marking, but a temporary table identifier must be used when the box is employed so that the video surveillance can accurately follow the box as it moves from the table to the count room.
- Paragraph (5) specifies that a drop box that has been removed from a gambling table must be stored in a secure area and afforded sufficient security to protect the drop box and its contents while awaiting the count. Again, as these boxes generally contain the majority of a cardroom's revenue, the boxes must be placed in a secure area to protect their contents from theft or tampering.
- Paragraph (6) allows unused drop boxes to be stored on gambling tables if the area is secure or covered by surveillance. Empty drop boxes are not at risk of content theft,

but could be at risk for tampering with the locks, etc. Therefore, even when empty, the boxes must be stored safely and securely. Having boxes locked to a gambling table in a secured area or under surveillance – either live or video – accomplishes this need for security. This broad standard allows lower tiers greater flexibility in satisfying this requirement.

- Paragraph (7) requires that licensees establish a schedule for the collection of drop boxes and ensure video recording of the entire drop box collection process. Provision is also included for deviation from the established collection schedule when necessary.

The collection process must be recorded by video surveillance to ensure that the boxes are collected appropriately and are not tampered with before they reach the count room to ensure the security of the box contents and satisfy the accounting and reporting requirements. The video will also document that the number of drop boxes collected is appropriate for the number of tables permitted to be in operation.

Deviation from the licensee's collection schedule may be necessary or appropriate in many situations that may not be predictable. For example, when the volume of play at a particular table is so great that the drop box is filled to capacity well before its scheduled collection time, an early collection would be necessary and appropriate to safeguard further drop fees for that table. On the other hand, an additional table put into play very close to a scheduled collection time may not have generated sufficient drop fees to warrant collection at the next scheduled time, so excluding that table from that collection may be appropriate. For that matter, on a particularly slow gambling day, there may not be sufficient drop fees generated at any table and skipping a scheduled collection time altogether during that shift may be reasonable. Furthermore, the unexpected absence of one or more of the employees designated to perform the drop collection may delay its commencement in order to locate a substitute. In view of these possible situations, it would be unreasonable not to allow deviation from an established drop collection schedule for good cause.

- Paragraph (8) requires that, for all licensees, the drop collection shall be performed by at least one licensed or permitted individual. Using licensed or permitted individuals will help to ensure the integrity of the drop collection process and protect the licensee's assets. Licensed and permitted employees are subjected to background checks in order to obtain a license or permit. Possession of a license or permit provides at least a minimum degree of confidence in the honesty, integrity and good character of the individual. This becomes an increasingly important factor as the potential for financial loss, and the size of the potential loss, increases as the tiers progress.

In addition, this requirement is consistent with the definition of a "gambling enterprise employee" in subdivision (n) of section 19805, which includes "collection personnel." Gambling enterprise employees are required, depending on the extent of



their duties and authority, to be either licensed or permitted. It follows, then, that the person or persons performing the drop collection must be licensed or permitted. The license/permit requirement applies to cardrooms in all tiers, but only one such individual is required for cardrooms in Tiers I and II. The size, both physical and fiscal, of these businesses, in general, does not necessarily warrant the use of more than one person to perform the drop collection and the owner licensees generally perform all the critical functions of cardroom operation in these tiers. The potential for loss is far less significant and requiring more than one person to perform the collection might necessitate hiring an additional, otherwise unneeded licensed or permitted employee in order to comply. On the other hand, Tier III and above licensees generally already have licensed and/or permitted employees that could be assigned this duty.

### **Tiers III-V**

- Subsection (b), paragraph (1) requires collection of all drop boxes, whether in use or not, at the same time. The collection is to be performed by, at a minimum, one key employee (licensed and not a security department employee) and one security department employee (may or may not be licensed or permitted). This requirement is intended to limit opportunities for collusion, safeguard the licensee's assets, and maintain the integrity of the drop collection process.
  - Paragraph (2) provides that the names of the individuals performing the drop box collection be documented either electronically (by computer software) or in writing and, if documented in writing, that the individuals print and sign their names in the documentation. Accurate documentation of each aspect of the drop collection process is necessary to maintain the integrity of the process, minimize opportunities for collusion, and safeguard assets.
  - Paragraph (3) allows unused drop boxes to be stored on gambling tables if the area is covered by recorded video surveillance. Again, empty drop boxes are not at risk of content theft, but could be at risk for tampering. Even when empty, the boxes must be stored safely and securely. Having boxes locked to a gambling table in a secured area and under recorded video surveillance satisfies this need for security. This slightly higher standard for Tiers III and above addresses the higher level of potential risk associated with the larger and largest gambling operations.
  - Subsection (c) requires the continuous live monitoring of the video surveillance recording of the drop box collection while in progress. This requirement is intended to control and enhance the security of the drop collection process and addresses the higher level of potential risk for losses associated with the largest gambling operations.
4. Adopt Section 12385 to establish the basic requirements for the maintenance and operation of count rooms that must be addressed in a licensee's policies and procedures. This section includes general specifications for the construction and security of count rooms, and the duties and activities of count room staff. In addition, this section will

establish the extent and complexity of these requirements as they apply to the licensee tiers established in Section 12380.

### **All Tiers**

- Subsection (a), paragraph (1), requires licensees to ensure that the counting and recording of the contents of drop boxes is accomplished in a manner that provides for appropriate security and proper accounting. Some cardrooms pay local taxes based upon their revenue. Therefore, the correct reporting of revenue is essential to meeting their appropriate tax liability. Similarly, some cardrooms have different state table fees based upon their income (Business and Professions Code section 19950), and so the proper income must be reported. This requirement is intended to assist in ensuring the accuracy of the count, to minimize the opportunity for theft and embezzlement, and to maintain the integrity of the count process.
- Paragraph (2) requires licensees to designate an individual or individuals, holding a license or permit, to perform the drop count. Using licensed or permitted individuals will help to ensure the integrity of the count process and protect the licensee's assets. Licensed and permitted employees are subjected to background checks in order to obtain a license or permit. Possession of a license or permit provides at least a minimum degree of confidence in the honesty, integrity and good character of the individual. This becomes an increasingly important factor as the potential for financial loss, and the size of the potential loss, increases as the tiers progress.
- Paragraph (3) requires that the count be recorded on a daily count sheet; specifies the information that must be recorded in a count sheet; and specifies how corrections are to be made when errors are identified in the recorded information. The daily count sheet documents the revenue of each drop box and maintains the integrity of the revenue accounting. This decreases the risk of under/over reporting of revenue.
- Paragraph (4) mandates the continuous recording of the count process by video surveillance. This requirement is intended to enhance security, minimize the opportunity for theft and embezzlement, and maintain the integrity of the count process.
- Paragraph (5) prohibits the mixing or commingling of the contents of one drop box with the contents of any other drop boxes prior to the count and recording of its contents. This prohibition is intended to assist in the accurate tracking of revenue for each shift, individual box and individual table.
- Paragraph (6) requires a drop box to be identified and the identity recorded when emptied and that recorded video surveillance document that all contents are removed from the box for the count. This requirement is intended to assist in creating an audit trail that will allow tracking of drop boxes from collection to the count. This will help to ensure the security and integrity of the count process and satisfy accounting and reporting requirements.

**Tiers II-V**

- Subsection (b), paragraph (1), requires licensees to maintain and use a secure area known as the “count room” to perform the count; that the area be designed and constructed to provide appropriate security; that it not be used for the storage of anything not directly associated with the count process; and, that it not house any removable containers that could be used to conceal chips or cash. This requirement is intended to provide enhanced asset safety and count process integrity for higher-tier gambling operations.
- Paragraph (2) provides that if the count room is used to store items or materials that are directly associated with the count (e.g., chips, cash or drop boxes), the interior of the room and its contents must be under constant recorded video surveillance. This provision is intended to allow licensees to make appropriate use of the count room for purposes other than, but related to the count process, while safeguarding the licensee’s assets and maintaining the safety and security of the room and its contents.

**Tiers III-V**

- Subsection (c), paragraph (1), provides that not less than two individuals be designated, pursuant to paragraph (2) of subsection (a), to perform the count, or one individual if an automated chip counting machine is used, as specified. This requirement is intended to limit opportunities for collusion, safeguard the licensee’s assets, and maintain the integrity of the count process.

This requirement that not less than two individuals perform the count begins with Tier III because the size of Tier I and Tier II cardrooms, both physical and fiscal, does not necessarily warrant this added level of protection. The potential for loss is far less significant and the owner licensees generally perform all the critical functions of cardroom operation. Adding this requirement for the lower tiers might necessitate hiring an additional otherwise unneeded employee in order to comply. On the other hand, Tier III and above licensees generally already have employees that could be assigned this duty.

The optional provision allowing one individual to perform the count if a count machine is used is intended to provide licensees with an alternative that may reduce labor costs without negatively impacting the safety of assets or the integrity of the count process.

- Paragraph (2) requires that the individuals performing the count wear clothing that reduces their ability to conceal chips on their person. This requirement is intended to reduce minimize the opportunity for theft, safeguard the licensee’s assets, and maintain the integrity of the count.
- Paragraph (3) requires a verification of the accuracy of the count by a cage or vault cashier after its conclusion. This requirement provides a means of identifying count errors in order to reduce the potential for under/over reporting of revenue, and it creates a documented audit trail.

- Paragraph (4) specifies that the count sheet must be immediately delivered to the accounting department following its verification and that the accounting department shall be responsible for maintaining and controlling the count sheets. This provision is intended to maintain the integrity of the count sheet by minimizing the opportunity for unauthorized alterations.

#### **Tiers IV-V**

- Subsection (d), paragraph (1), provides that the count room shall be a fully enclosed room with an alarm system connected to all doors to the room that signals the security unit whenever any door to the count room is opened. This provision is intended to establish an enhanced level of protection for licensee's assets commensurate with the increased potential risk found in the higher tier gambling establishments. Both the larger size of their establishments and the significantly higher amount of their revenue warrant a higher degree of protection.
- Paragraph (2) requires that one of the designated individuals notify the surveillance unit immediately prior to commencement of the count and that the entire count be continuously monitored and recorded by video surveillance. This requirement is intended to provide added assurance that the video monitoring and recording of the entire count process will take place in order to ensure the safeguarding of assets and maintain the integrity of the count.
- Paragraph (3) provides that access to the count room shall be secured prior to the opening of any drop box and that the exit and entrance of individuals be controlled until the count process, including recording and verification, is completed. In keeping with the increased potential risk found in the higher tier gambling establishments, this provision is intended to enhance the level of protection for licensee's assets.

#### **Tier V**

- Subsection (e) provides that not less than three individuals be designated, pursuant to paragraph (2) of subsection (a), to perform the count, or two individuals if an automated chip counting machine is used, as specified. This provision is intended to enhance the safety and security of the count process and addresses the higher level of potential risk of losses associated with the largest gambling operations.
5. Adopt Section 12386 to establish the basic requirements for the maintenance and operation of cages that must be addressed in a licensee's policies and procedures. This section includes specifications for the construction and security of cages, and the duties and activities of cage staff. In addition, this section will establish the extent and complexity of these requirements as they apply to the licensee Tiers established in Section 12380.

#### **All Tiers**

- Subsection (a), paragraph (1), provides that licensees shall ensure the appropriate security and accountability of funds by the maintenance of an area within the

gambling establishment, as specified, that is designated as the cage. The cage is the main area of a cardroom where cash is kept, as patrons exchange their cash for chips, cash checks, or access their players' banks from the cage. In addition, patrons often fill out required IRS forms or credit request forms at the cage, which are kept in the cage until transmitted to the accounting department. Thus, both cash and sensitive information are kept in this area. Therefore, it is necessary to keep this area secure, including video surveillance and restrictions on access to non-authorized personnel, as well as internal controls such as segregation of duties involving reconciling cash drawers.

- Paragraph (2) requires that at least one employee be designated to process transactions through the cage and specifies the duties and responsibilities of that position. This requirement is intended to ensure that each employee assigned to work in the cage is identified and the designation documented; and that the general duties and responsibilities that those employees may be held accountable for are clearly identified. This is a basic element in safeguarding the licensee's assets and protecting sensitive and confidential information that may be present in the cage.
- Paragraph (3) provides that access to the cage shall be limited, restricted and controlled. Both cash and sensitive/confidential information are kept in this area. Restricting access to authorized personnel and controlling access by non-authorized personnel assists in ensuring the security of the area. This provision is intended to reduce the risk of loss or inappropriate access to sensitive or confidential information and/or documents.
- Paragraph (4) requires that a log be maintained, as specified, to document entry into the cage area by anyone other than authorized, on-duty cage personnel, and that any automated access control system record substantially the same information specified for the manual log. This is another factor that assists in preserving the security of the cage area and safeguarding its contents. Should issues arise, the log will document who, in addition to authorized, on-duty cage personnel, was granted access to the cage at any time relating to the issue.
- Paragraph (5) requires that a reconciliation of the cage activity be performed at the end of each shift by both the incoming and outgoing designated cage employees; that if an impress is used, the outgoing employees reconcile their drawers to the impressed amount; that all transactions be appropriately summarized and documented, as specified; and that the cage activity reconciliations be posted and reconciled to the general ledger monthly. Regular reconciliations and postings are a critical element in any financial accounting system and are a basic minimum internal control standard in any fiscal operation. Regularly occurring reconciliations of transactions confirm the accuracy of the accounting system, timely identify irregularities and errors, and support the credibility of financial reporting. By requiring both the outgoing and the incoming cashiers to perform the shift-change reconciliation, shift-to-shift continuity is established and confirmed, and each cashier is assured of the accuracy and consistency of the amounts they are receiving and transferring. However, in the case

of an impress, each cashier is responsible for his or her own drawer or bankroll. Therefore, there is no need for incoming and outgoing cashiers to be involved in each other's reconciliations.

- Paragraph (6) specifies that a patron may only purchase or redeem chips from the cage or a designated employee on the gambling floor, and prohibits the purchase or redemption of chips from patrons by third-party proposition player service providers. Clarification is also included that provides that changing or breaking chips (e.g., exchanging a \$50 chip for 10 – \$5 chips) is not prohibited, whether at a cage, with a dealer or between players. This requirement is intended to assist in assuring compliance with Title 31 of the United States Code, and to minimize the potential for the introduction of counterfeit chips and/or currency into the gambling establishment.

### **Tiers III-V**

- Subsection (b), paragraph (1), requires continuous recorded video surveillance of the cage and cage activities. This requirement is intended as an enhancement to provide added protection of assets, greater assurance of the integrity of the cage and cage employees, thus minimizing the opportunity for theft.
- Paragraph (2) requires a summarization of the reconciliation of cage transactions (see (a)(5) above) on a cage accountability form and specifies the information that must be included in that form. This requirement is intended to enhance the accuracy and consistency of the end-of-shift cage reconciliation by specifying the basic information that is to be summarized and recorded.
- Paragraph (3) provides that the cage activity reconciliation shall be posted to a general ledger at least monthly by someone other than a cage employee or supervisor. This provision is intended to assist in preserving the integrity of the reconciliation and minimize the opportunity for collusion through a clear separation of duties.

### **Tiers IV-V**

- Subsection (c), paragraph (1) specifies that the cage must have a manually triggered silent alarm; that the cage access door(s) be secured; and, that the door(s) be under constant recorded video surveillance. The alarm requirement is intended to provide for notification of law enforcement in the event of a robbery. The securing and recorded video surveillance of doors is intended to provide greater access control and enhanced security for the cage. These provisions are intended to further safeguard assets by establishing enhanced requirements appropriate to the higher degree of risk associated with the larger gambling operations.
- Paragraph (2) requires a summarization of the reconciliation of cage transactions (see (a)(5)) on a cage accountability form (see (b)(2)) that includes additional information, as specified. This requirement is intended to further enhance the accuracy and consistency of the end-of-shift cage reconciliation by requiring additional detail that may only be necessary and appropriate for the higher tier gambling establishments.

- Paragraph (3) requires that licensees maintain a list of designated persons that have been authorized access to the cage. The list shall also indicate who possesses the combination or keys to the devices securing the cage and who can access and operate the cage alarm. This requirement is intended to ensure that each employee assigned to work in, or authorized access to the cage is identified and that the assignment and/or authorization be documented. This serves to enhance the accountability of individuals, to document segregation of duties, and to clearly identify and document who may control physical access to the cage. These provisions are intended to further safeguard the licensee's assets and protect sensitive and confidential information by establishing enhanced requirements appropriate to the higher degree of risk associated with the larger gambling operations.

**Tier V**

- Subsection (d) requires that the interior of the cage and all of its contents, as well as the exterior of all cage access doors, be under monitored and recorded video surveillance. This requirement is intended as a further enhancement to the basic video surveillance requirement in order to provide added protection of assets and greater assurance of the integrity of the cage and cage employees, commensurate with the higher level of potential risk of losses associated with the largest gambling operations.
6. The proposed action will also require licensees to establish and implement the applicable standards specified in Sections 12384, 12385 and 12386 by a date certain (approximately six months after the effective date of those regulations). This will provide licensees with adequate notice and sufficient time to develop appropriate policies and procedures in compliance with the newly adopted standards and requirements.

**UNDERLYING DATA:**

Technical, theoretical or empirical studies or reports relied upon:  
None.

**BUSINESS IMPACT:**

The Commission has made an initial determination that the proposed regulatory action may have a significant statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states, if those affected businesses do not already have internal control standards in place which satisfy the minimum standards proposed by these regulations.

**SPECIFIC TECHNOLOGIES OR EQUIPMENT:**

The proposed regulatory action does not mandate the use of specific technologies or equipment.

**CONSIDERATION OF ALTERNATIVES:**

No reasonable alternative to the regulation would be either more effective in carrying out the purpose for which the action is proposed or would be as effective and less burdensome to affected private persons than the proposed regulation.

Set forth below are the alternatives that were considered and the reasons each alternative was rejected:

No reasonable alternative has been considered or otherwise identified and brought to the attention of the Commission.