CALIFORNIA GAMBLING CONTROL COMMISSION

Amended Detailed Response to Tribal-State Association Objections to Internal Control Standards (CGCC-8) September 10, 2009

Compact section 8.4.1, and comparable sections of the new or amended Compacts, (Compact) sets out procedures for the State Gaming Agency (SGA) to propose uniform statewide regulations governing Class III Gaming Operations and for the Association of Tribal and State Gaming Regulators (Association) to approve or disapprove them. Section 8.4.1 (b) provides that the SGA may re-adopt a regulation in its original or amended form after disapproval by the Association, and then submit the regulation to each individual Tribe, provided that the SGA prepares a detailed, written response to the Association's objections.[1],[2] Compact section 8.4.1(e) states that Tribes may object to a proposed statewide uniform regulation on any of four enumerated grounds: that is, that the regulation is "unnecessary, unduly burdensome, conflicts with a published final regulation of the [National Indian Gaming Commission], or is unfairly discriminatory . . . ."

At its September 4, 2008 meeting, the Association voted to disapprove the proposed regulation CGCC-8, regarding Minimum Internal Control Standards (MICS), based upon the objections stated in the Association Task Force Report, dated February 13, 2008 and in letters received within 14 days of the vote.[3] The Commission met on October 14, 2008 where it re-adopted CGCC-8 as a proposed regulation. Soon thereafter it sent the October 14, 2008 version of CGCC-8 to the Tribes asking for comments. Between that date and September 4, 2009, the Commission has considered setting two hearings to adopt CGCC-8 as final. However, in response to concerns and suggestions raised in comments, the Commission did not schedule the

[1] Compact section 8.4.1, subsection (b) provides

> "Every State Gaming Agency regulation that is intended to apply to the Tribe (other than a regulation proposed or previously approved by the Association) shall be submitted to the Association for consideration prior to submission of the regulation to the Tribe for comment as provided in subdivision (c). A regulation that is disapproved by the Association shall not be submitted to the Tribe for comment unless it is *readopted* by the State Gaming Agency as a proposed regulation a proposed regulation in its original or amended form with a detailed written response to the Association's objections." (Emphasis added.)

[2] The State believes that section 8.4.1, subsection (b) provides a clear exception to the general proposition in subsection (a) of 8.4.1 that the regulation has to be approved by the Tribal-State Association. This readoption and response procedure constitutes an exception to the general requirement that the Association approve a regulation before it may be effective. Any other interpretation would render subsection (b) mere surplusage, and such a construction must be avoided. (*Boghos v. Certain Underwriters at Lloyd's of London* (2005) 36 Cal.4th 495,503 [language in a contract must be interpreted as a whole and constructions that render contractual provisions surplusage are disfavored].)

[3] The motion made at the meeting was to oppose the adoption of the CGCC-8 regulation based on the objections in the Task Force Report of February 13, 2008.

hearing until September 24, 2009. The Association has also scheduled a hearing for September 17, 2009 where the new Task Force report and Draft of CGCC-8 will be considered.[4]

The following Tribes, TGAs, or Commissions sent in comments in advance of September 4, 2009 over the course of three separate time frames. First, the Commission received the following comments after the conclusion of the October 14, 2008 Re-Adoption of CGCC-8, but before the April 15, 2009 Staff Draft was sent out: 1) Steve Wilson, Chairman, Mooretown Gaming Commission; 2) David Hawkins, Chairman, Pit River Gaming Commission; 3) Glenn M. Feldman, Esq., Representing Cabazon Band of Mission Indians, Santa Ynez Band of Chumash Indians, and San Pasqual Band of Mission Indians; 4) Melvin Jackson, Vice Chairman, Mooretown Gaming Commission; 5) Marshall McKay, Chairman, Rumsey Band of Wintun Indians; 6) Jessica Tavares, Chairperson, United Auburn Indian Community; 7) Leanne Walker-Grant, Tribal Chairperson, Table Mountain Rancheria; 8) Robert Smith, Chairman, Pala Band of Luiseno Mission Indians of the Pala Reservation; 9) Garth Sundberg, Chairman, Cher-Ae Heights Indian Community of the Trinidad Rancheria; 10) Armando T. Ramos, Gaming Commission Chair, San Manuel Band of Mission Indians Tribal Gaming Commission; 11) Everett Freeman, Chairman, Paskenta Band of Nomlaki Indians; 12) Irwin "Bo" Marks, Vice Chairman, Jackson Rancheria Band of Miwuk Indians of the Jackson Rancheria; 13) Mark Macarro, Chairman, Pechanga Band of Luiseno Mission Indians; 14) Neil Peyron, Chairman, Tule River Tribal Council; 15) Kevin A. Day, Chairman, Tuolumne Band of Me-Wuk Indians; 16) Gwendolyn Parada, Chairperson, La Posta Band of Mission Indians; 17) Dale A. Miller, Chairman, Elk Valley Rancheria; 18) Valentino Jack, Chairman, Big Valley Band of Pomo Indians; 19) Michael Lombardi, Chairman, Augustine Gaming Commission; 20) Mr. Stacy Dixon, Tribal Chairman, Susanville Indian Rancheria; 21) Darrell Mike, Chairman, Twenty-Nine Palms Band of Mission Indians; 22) Morris Reid, Chairman, Picayune Rancheria of the Chukchansi Indians; 23) George Forman, Attorney, Representing Robinson Rancheria of Pomo Indians; 24) Lenora "Dee" Cline, President, Pauma Gaming Commission; 25) Elizabeth Kipp, Chairperson, Big Sandy Rancheria; 26) Larry Sisco, Chairman, and Fabian Barrios, Commissioner, Santa Rosa Rancheria; 27) Bo Mazzetti, Vice-Chairman, Rincon Band of Luiseño Indians; 28) Robert Martin, Chairman, Morongo Band of Mission Indians; 29) George Forman, Attorney, Representing Cachil Dehe Band of Wintun Indians of the Colusa Indian Community; 30) Michael Castello, Chairman, Soboba Tribal Gaming Commission; 31) Monty Bengochia, Chairman, Bishop Tribal Council; 32) Kara Brundin Miller, Tribal Chair, Smith River Rancheria; 33) Chris Devers, Chairman, Pauma Band of Mission Indians; 34) Richard M. Milanovich, Chairman, Agua Caliente Band of Cahuilla Indians; 35) George Foreman, Attorney, Representing Sycuan Band of the Kumeyaay Nation; 36) Harvey Hopkins, Chairman, Dry Creek Rancheria Band of Pomo Indians; and 37) Rick Dowd, Chairman, Coast Indian Community of the Resighini Rancheria. These comment letters are attached as Exhibits "A1-A37" respectively.

Second, the Commission received the following comments after the April 15, 2009 Staff Draft of CGCC-8 was sent out but before the Task Force Draft was completed and sent out: 1) United Auburn Indian Community, Jessica Tavares, Chairperson; 2) Pala Band of Mission Indians,

[4] A more thorough regulatory history is available in the accompanying Staff Report with its Summary of Comments and Changes to CGCC-8.

Robert Smith, Chairman; 3) Rincon Band, Bo Mazzetti, Chairman; 4) Rumsey Indian Rancheria, Marshall McKay, Chairman; 5) Bishop Paiute Tribe, Monty Bengochia, Chairman; 6) Soboba Band of Luiseno Indians, Jay Shapiro, Forman & Associates; 7) Tule River Gaming Commission, Teri Carothers, Vice Chairperson, Amy McDarment, Secretary/Treasurer; 8) San Manuel Band of Mission Indians, Armando Ramos, Gaming Commission Chair, Julian Abarca, Gaming Commissioner, Robert Balderama, Gaming Commissioner; 9) Big Sandy Rancheria, Elizabeth Kipp, Chairperson; 10) Pauma Band of Mission Indians, Chris Devers, Chairman, Lenora "Dee" Cline, President; 11) Cabazon Band of Mission Indians, Santa Ynez Band, and San Pasqual Band of Mission Indians, Glenn Feldman; 12) Alturas Rancheria, Philip Del Rosa, Chairman; 13) Paskenta Band of Nomlaki Indians, Everett Freeman, Chairman; 14) Chukchansi Indians, Morris Reid, Sr., Chairman, Mark Emerick, Secretary; 15) Susanville Indian Rancheria, Ginny Morales, Chairperson; 16) Tuolumne Me-Wuk Tribal Council, Kevin Day, Chairman; 17) Mooretown Rancheria, Steve Wilson, Chairman; 18) Cachil Dehe Band of Wintun Indians of the Colusa Indian Community, George Forman, Attorney. These comment letters are attached as Exhibits "B1-B18" respectively.

Third, the Commission received the following comments after the Task Force Draft of CGCC-8 was sent out on August 7, 2009, but before the September 4, 2009 Deadline in advance of hearing on CGCC-8: 1) Picayune Rancheria of the Chukchansi Indians, Morris Reid, Chairman, Two Letters; 2) La Posta Band of Mission Indians, Gwendolyn Parada, Chairperson; 3) Rincon Band of Luiseño Indians, Stephanie Spencer, Vice Chairwoman, Gilbert Parada, Council Member, Charlie Kolb, Council Member, Steve Stallings, Council Member; 4) Santa Rosa Rancheria, Ruben Barrios Sr., Tribal Chairman; 5) Cahuilla Band of Indians, George Forman, Attorney; 6) Robinson Rancheria Band, George Forman, Attorney; 7) Tuolumne Band of Me-Wuk Indians, Kevin A. Day, Chairman; 8) Big Sandy Rancheria, Elizabeth D. Kipp, Tribal Chairperson; 9) United Auburn Indian Community, Jessica Tavares, Chairperson; 10) Morongo Band of Indians, George Forman, Attorney; 11) Tule River Tribal Council, Ryan Garfield, Chairman; 12) Paskenta Band of Nomlaki Indians, Everett Freeman; 13) Pauma Band of Mission Indians, Chris Devers, Chairman, Lenora "Dee" Cline, President, Pauma Gaming Commission; 14) Elk Valley Rancheria, Dale A. Miller, Chairman; 15) Mooretown Rancheria, Gary W. Archuleta; 16) Dry Creek Rancheria, Vicki Wattles, Chairperson; 17) Susanville Indian Rancheria Gaming Commission, Ginny Morales, Chairperson; and 18)Rumsey Indian Rancheria, Tribal Gaming Agency, Leland Kinter, Chairman. These comment letters are attached as Exhibits "C1-C18" respectively.

This document is the written response to the Association's objections as required by Compact subsections 8.4.1(b)&(c). It includes the rationale for the CGCC-8 text (dated September 10, 2009) and a detailed response to the objections raised by Tribes, the Association, and the Task Force.[5] The Commission's Responses to the February 2008 Task Force Report dated April 23, 2008, and Response to Association's objections dated October 9, 2008 and supplemental are also incorporated herein. (Attached as Exhibits "D" and "E1" and "E2".)

[5] The Task Force created another report in August 2009 which included a revised version of CGCC-8. This subsequent report largely referenced and incorporated the original Task Force report as a basis and all references contained herein are to the 2008 Task Force Report.

At the outset, it is apparent that the Commission's earlier responses have been revised in several areas. These alterations are made as a direct result of beneficial Tribal comments, extensive interaction through the course of meetings with Tribal attorneys, the recent Task Force, as well as through analyzing the Task Force's August 6, 2009 draft of CGCC-8. Making alterations in CGCC-8 and throughout this Response in light of these comments should not be construed as a reversal of the Commission's prior position on these issues or as concessions that previous positions were invalid. This is not the case. Rather these revisions should be viewed for what they are: concrete signs of the Commission's willingness to engage actively California Compacted Tribes in the regulatory process through government to government relations and the respect of mutual sovereignty. These interactions are paramount to the regulatory process and have occurred over the course of more than two years. The result is a version of CGCC-8 that is more focused, clearer as to protocols of inspection, continues to encourage uniformity, provides for Tribal Alternatives, protects both the Tribe's and the State's Compact interests, and allows the beneficial communication made during the course of drafting this regulation to continue through its enactment and utilization.

PART I. RATIONALE FOR INTERNAL CONTROL STANDARDS

(CGCC-8 amended form dated September 10, 2009)

1. INTRODUCTION

Internal controls are the primary procedures used to protect the integrity of casino gaming operations, which is cash intensive, and are a vitally important part of properly regulated gambling. Inherent in gaming operations are problems of customer and employee access to cash, unrecorded cash transactions at table games, manipulation of credit, questions of fairness of games, and the threat or risk of collusion to circumvent controls.[6] Internal control standards are therefore commonplace in the gambling industry and many Tribes in California currently have some standards in place.

> Inherent in an internal control structure are the concepts of individual accountability and segregation of incompatible functions. The existence of standards alone, however, is not enough. Any internal control system carries the risk of circumvention, which is why a process of *independent* oversight is so critical to the integrity of an operation. (Emphasis added.)[7]

Under IGRA, a Tribe conducts Class III gaming pursuant to a compact with the State. (See 25 U.S.C. § 2710(d)(1)(c).) After the Secretary of the Interior approves the compact, the "*Tribal-*

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[6] The most recent totals for the United States Indian gaming revenue for 2007 stood at over $26 billion. Source: *NIGC Strategic Plan for Fiscal Years 2009-2014*, page four. The link is http://www.nigc.gov/LinkClick.aspx?fileticket=gruAugiyc28%3d&tabid=36&mid=345. Page four of the Plan is included as Exhibit "F."

[7] Written Remarks of National Indian Gaming Commission Chairman Montie R. Deer before the Senate Committee on Indian Affairs, March 14, 2002. (See complete remarks attached as Exhibit "G.")

State compact govern[s] the conduct of [class III] gaming activities" § 2710(d)(3)(A) (emphasis added), and the Tribes's class III gaming operations, including standards for operation, must be "conducted in conformance" with the compact, § 2710(d)(1)(C) and § 2710(d)(3)(C)(vi) and (vii).

2. NATIONAL INDIAN GAMING COMMISSION MICS

The National Indian Gaming Commission (NIGC) Minimum Internal Control Standards ("NIGC MICS"), were designed to establish a baseline, that is, **minimum** internal control standards, to be required of Tribal Gaming Operations. Initially adopted in 1999, the NIGC MICS have been amended over the years to take into account advances in technology, and to clarify certain requirements. They were intended to embody accepted industry practices.[8]

The NIGC MICS are structured by size of gaming operations rather than by type of game, thus recognizing that the requirements placed upon tribal gaming operations should differ based upon their annual gross gaming revenue. Costs involved in implementing controls are part of the regular business costs incurred by a Gambling Operation. Because different states have different compacts as to types of games offered (such as craps, roulette, or pari-mutuel wagering) or as to credit, or because certain Tribes opt not to offer particular games or extend credit, the NIGC MICS cover some areas not applicable to all Tribes. However, as long as the Tribal internal controls met or exceeded the standards in the NIGC MICS for the applicable areas, uniform standards were achieved.

3. THE *COLORADO RIVER INDIAN TRIBES* (*CRIT)* DECISION

In *Colorado River Indian Tribes v. National Indian Gaming Commission (CRIT),* 466 F.3d 134, decided October 20, 2006, by the United States Court of Appeals for the District of Columbia Circuit, the court held that NIGC did not have the authority to promulgate or enforce the NIGC MICS with regard to Class III gaming. This decision effectively eliminated the Federal government's authority and jurisdiction to regulate Class III gaming in California, at least with regard to the Class III NIGC MICS. The court clearly held that the declared policy of shielding Indian Tribes "from organized crime and other corrupting influences" and "to assure that gaming is conducted fairly and honestly by both the operator and players" for Class III gaming is accomplished through the only allowable statutory basis for such, through the Tribal-State compacts. (*CRIT*, *supra,* 466 F.3d, at p. 140; emphasis added.) The existing framework under IGRA of Tribal-State Compacts establishing the regulatory rules for Class III gaming did not change with the *CRIT* decision.

4. THE AUTHORITY OF THE STATE GAMING AGENCY

The Preamble to the Compact provides that the Compact is made pursuant to IGRA and that the system of regulation fashioned by Congress in IGRA rests on an allocation of regulatory jurisdiction among three sovereigns – the Federal government, the State, and the Tribe. The Compact recognizes the State's interest in ensuring, jointly with the Tribes, that "tribal gaming activities are free from criminal and other undesirable elements" (Compact Preamble, paragraph

[8] *See* Written Statement of National Indian Gaming Commission Chairman Philip N. Hogen before the Senate Committee on Indian Affairs, June 28, 2007. Exhibit H

(F)). One of the stated Purposes and Objectives of the Compact is to ensure that Tribal Class III gaming is "conducted fairly and honestly by both the operator and players" (Compact Preamble, paragraph A). See also Compact section 1(b) (compact purpose is to ensure "fair and honest operation" of Class III gaming in accordance with IGRA).

The primary responsibility for regulating the Gaming Operation rests with the Tribe and the TGA. Specifically, the Tribe must adopt a gaming ordinance and conduct its gaming activities in compliance with that ordinance and rules, regulations, procedures, specifications, and standards adopted by the Tribal Gaming Agency (TGA). In addition to oversight by the TGA, NIGC has in the past performed the valuable role of providing independent outside oversight, as in the area of NIGC MICS compliance review.

However, in addition to the Tribe and the TGA, the SGA also has a role and has the authority to promulgate regulations to establish statewide uniform operating procedures. Section 8.0 of the Compact is entitled "Rules and Regulations for the Operation and Management of the Tribal Gaming Operation." Section 8.1 of the Compact is entitled "Adoption of Regulations for Operation and Management: *Minimum Standards*." (Emphasis added.) Section 8.1 states that each TGA must adopt rules, regulations, and specifications concerning, *at a minimum*, thirteen enumerated topics "and to ensure their enforcement in an effective manner." (Emphasis added.) Section 8.4 (no title) provides in substance as follows:

1. That the parties agree that the SGA, for the purpose of fostering "statewide uniformity of regulation of Class III gaming operations throughout the state," has the power to adopt regulations on "any matter encompassed by Section 6.0, 7.0. and 8.0". (Emphasis added.)

2. That the rules, regulations, standards, specifications, and procedures adopted by the TGA "shall be consistent with regulations adopted by the State Gaming Agency in accordance with Section 8.4.1." [9]

Essentially, statewide uniform regulations under Compact section 8.4 can encompass any matter within Compact sections 6.0, 7.0 and 8.0, and the TGA rules, regulations and standards must be consistent with statewide uniform regulations adopted by the SGA. Compact section 7.1 requires the TGA to adopt and enforce regulations which ensure that the Gaming Operation "meets the highest standards of regulation and internal controls." Section 8.1 charges the TGA with responsibility to promulgate such rules, regulations and specifications and to ensure their enforcement. Compact sections 8.1.1 through 8.1.14 outline the matters which, at a minimum, these rules, regulations, and specifications must address. Compact sections 7.4 through 7.4.4

[9] Compact Section 8.4 provides in full:

> " In order to foster statewide uniformity of regulation of Class III gaming operations throughout the state, rules, regulations, standards, specifications, and procedures of the Tribal Gaming Agency in respect to any matter encompassed by Sections 6.0, 7.0, and 8.0 shall be consistent with regulations adopted by the State Gaming Agency in accordance with Section 8.4.1. Chapter 3.5 (commencing with section 11340) or Part 1 of Division 3 of Title 2 of the California Government Code does not apply to regulations adopted by the State Gaming Agency in respect to tribal gaming operations under this section." (Emphasis added.)

provide the SGA the right to inspect the Gaming Facility, and Gaming Operation or Facility records, as defined in the Compact, as to ensure compliance with the Compact. The purpose of this regulation (CGCC-8), pursuant to section 8.4, is to provide an effective uniform manner in which the SGA can conduct compliance inspections of the adoption and enforcement of these rules, regulations, and specifications by the TGA (Tribal MICS), and to protect the public as well to assist the Tribe and the TGA.

In light of the fundamental importance of MICS in protecting the integrity of Tribal Gaming Operations, notably Class III Gaming Activities, it is appropriate for the SGA to encourage through regulation the TGA's adoption of uniform, minimum requirements for Tribal MICS: that is, the TGAs' adoption of Tribal MICS which equal or exceed the NIGC MICS as promulgated by the NIGC as of October 1, 2006, and to reiterate the Compact's requirement that each Tribal Gaming Operation implement internal control systems that ensure compliance with the Tribal MICS.

The California Gambling Control Commission (Commission) has specific responsibilities under the Tribal-State Gaming Compacts, including the auditing of Tribal contributions to the General Fund, Special Distribution Fund, and Revenue Sharing Trust Fund. The Commission has the right to verify the proper receipt of money due to the State under the Compacts, and ensure that the State's interest in this revenue stream is protected. The NIGC MICS and Tribal MICS are integral to these obligations and help ensure that revenue is both reported and also provides the ability to check the accuracy of the numbers. Pursuant to the Compact, the State has access to the Gaming Operation and to copy papers, books, and records related thereto. (See Compact, Sec. 7.4.) Among those books and records available for inspection are those related to the matters set forth in Sec. 8.0 of the Compact. Among those matters in 8.0, certain sections are items related to Tribal MICS. (See, for example, Compact Secs. 8.1 – 8.1.14, inclusive, which cover such things as "employee procedures designed to permit detection of irregularities, theft, cheating or fraud", and "maintenance of closed-circuit television surveillance system" and "cashier's cage.") It also has the right to access other areas where reasonably necessary to ensure compliance with the Compact. (See Compact, Sec. 7.4.4.) Therefore, the Commission has the authority under the Compact to inspect all books and records relating to a Tribe's MICS.

For a variety of reasons, including the presence of the Federal government assuming a prominent regulatory role, the State's oversight and auditing have to date been more focused on the Revenue Sharing Trust Fund, the Special Distribution fund, and, under new and amended compacts, contributions to the General Fund.[10] Now, with the determination that the Compact provides the exclusive authority for Class III MICS regulation, the State must turn its attention to

[10] The Commission in 2003 did perform reviews of MICS compliance as it related to several areas of Class III gaming devices and revenues as part of net win and fund contribution audits. The Commission utilized the NIGC Check lists as work paper guidelines. However, due to the priority of other Compact issues and limited resources, the Commission was not able to continue to perform complete reviews of all MICS compliance topics and streamlined the NIGC checklists and areas reviewed. Financial Audits staff subsequently did and continues to look at areas of internal controls critical to Class III gaming device net win and some of those controls are captured in MICS compliance. Beginning in Budget year 2007-2008, the Commission received sufficient budget resources to begin full Class III internal control audits and implemented full MICS inspections beginning in the spring of 2008.

these Compact authorized inspections of Tribal Gaming Operations to help the TGA and Tribe ensure the integrity of the Gaming Operation for the public, thus CGCC-8.

5. CGCC-8 -- INTERNAL CONTROL STANDARDS

CGCC-8 establishes uniform basic standards and protocols for State inspection of Tribal regulation of Gaming Operations. It does this by establishing the NIGC MICS as a baseline for Compact-compliant Tribal MICS. Using the NIGC MICS as a baseline "Standard of Compliance" ensures consistency and uniformity while taking into account the size of Gaming Operations. Further, since many Compacted Tribes reportedly helped create these standards and followed them for years, this approach eliminates duplication or unnecessary promulgation of new rules, regulations, or specifications under the Compacts' requirement for internal controls.

The State has significant oversight and inspection authority as outlined above. CGCC-8 is not an expansion of that authority, but rather recognition that the authority existed all along, and is thus simply an exercise of that authority. In addition, in the spirit of respecting Tribal sovereignty, CGCC-8 creates a second category for "Material Compliance" where a TGA may also adopt Tribal MICS that exceeds the NIGC MICS. These Tribal MICS will be considered Compact compliant. In addition, Tribes and TGAs may wish to adopt Tribal MICS that are entirely different than the NIGC MICS. These *may* also be Compact compliant, but further SGA inspection may be necessary under the Compact. Thus, this regulation has been drawn as narrowly as possible to respect Tribal sovereignty, while still protecting the integrity of Tribal Gaming Operations in California by encouraging uniformity via adoption of the NIGC MICS.

Additionally, CGCC-8 goes further to establish protocols beneficial to the Tribe for how the SGA exercises its rights under Compact section 7.4, including requirements such as notice, interaction over reports, reviews to the full Commission, entrance and exit conferences, confirmation of dispute resolution proceedings, etc. CGCC-8 also reiterates the provisions in existing Compacts that utmost care will be exercised in regard to protecting the confidentiality of information provided by the Tribe. The extent of the information being shared under this regulation is generally the same as what the Tribes were sharing with the Federal government, and thus no new or additional information is being shared with an outside (non-tribal) governmental agency. In any event, access to such information is currently provided by the compact. Finally, CGCC-8 recognizes some Tribe's efforts to re-establish NIGC MICS reviews with an Alternative Compliance section which includes minimum requirements necessary to allow the SGA to fulfill its role under the Compact. Mandating anything less than these minimal requirements would require a Compact amendment.

6. OTHER FACTORS MENTIONED IN THE PROTOCOL CRITERIA

(i) **Economic Impact**. This proposed regulation should have no additional economic impact, since many Tribes have been complying with the NIGC MICS since 1999 or have some form of internal control standards because they are considered essential under industry practice for protecting gaming assets. Thus, this regulation is not unduly burdensome.

Furthermore, for Tribes who follow the "Standard of Compliance" or are materially compliant with adoption of the NIGC MICS as their Tribal MICS or Tribal MICS that meet or exceed the NIGC MICS, Gaming Operations are tiered by revenues, with tighter and more controls imposed as the revenues increase.[11] NIGC indicated in its Final Rule Revisions 25 CFR Part 542, 71 Fed. Reg. 277385 (May 11, 2006) at p. 27390, that the cost of compliance with the requirement for independent certified public accountant testing will , for small gaming operations, be between $3,000 and $5,000. This testing measures the Gaming Operation's compliance with the Tribe's internal control standards. This cost, according to NIGC, is "relatively minimal" and "does not create a significant economic effect on gaming operations" and what little effect there is can be offset by performing the required yearly independent financial audit at the same time.

Furthermore, for Tribes that seek to be covered under "Material Compliance" with Alternative Tribal MICS, this regulation would have minimal economic impact as the Tribal MICS would be adopted according to the TGA's discretion as to the Gaming Operations. These are already required under the Compact, and this regulation has no additional cost. Therefore, for these reasons, these proposed regulatory standards do not disparately impact small operations over large operations, and this regulation will not have significant economic impact. The regulation is thus not unduly discriminatory amongst Tribes.

(ii) **Application outside Tribal Gaming**. CGCC-8 is not "unduly discriminatory" against Tribes vis-a-vis others in the gaming industry, such as cardrooms and racetracks. California cardrooms (gambling establishments) are governed not only by numerous provisions of the Penal Code[12] and the Business and Professions Code,[13] but also by regulations adopted by the Commission[14] and by the Department of Justice, Bureau of Gambling Control.[15] Strict regulations are in place concerning cardroom accounting and financial reporting.[16] In addition, the Commission is in the process of enacting a variety of additional regulations, specifically dealing with MICS issues. The first MICS regulation governed the extension of credit, check cashing and automatic teller machines (ATMs). The second MICS regulations governed drop & drop collection; count & count room functions; and cage functions. Currently, the

[11] Under the NIGC MICS the provisions do not apply to operations that have gross revenues under $1 million. Tier A facilities are those with gross revenues between $1 and $5 million; Tier B facilities are those with gross revenues of more than $5 but not more than $15 million; and Tier C facilities are those with gross revenues of more than $15 million.

[12] See, for example, Penal Code sections 337j (e) (defining "controlled game") and 330 (listing prohibited games).

[13] The Gambling Control Act, Business and Professions Code sections 19800-19987.

[14] Commission regulations are found in Title 4 CCR sections 12002-12590.

[15] Bureau regulations are found in Title 11 CCR sections 2000-2142.

[16] See CGCC regulations at Title 4 CCR sections 12400—12406.

Commission is working on a third set of MICS regulations on security and surveillance, which are in the final stages of the rulemaking process. These are projected to be effective in February 2010. In addition, the Commission is also working on gambling floor operations and the play of table games which ideally will be effective mid-2010. Finally, the Commission will soon commence preparation of MICS regulation of chips, cards and other gaming equipment which ideally will be effective in late 2010.

In addition, beyond the context of MICS, Cardrooms must, for example, maintain records of the drop for each table for a period of seven years, which records must be provided upon request to the State. The chart of accounts used in each cardroom's accounting system must be approved by the Commission.[17] All cardrooms with a gross annual revenue of $10 million or more must have an annual audit done by an independent California CPA, a copy of which audit must be provided to the State, along with the management letter and reply to the management letter, if any.[18] Cardrooms with a lower annual gross revenue may be directed to have an audit performed if the State has concerns about the licensee's operation or financial reporting, including, but not limited, to inadequate "internal control procedures."[19] Moreover, the State may require the cardroom to have a fraud audit performed by an independent CPA in the event that fraud or illegal acts are suspected.[20]

As the Tribes are aware from their reported participation in the creation of the NIGC MICS, the MICS drafting process takes years to complete and with substantial dialog between interested parties. IGRA was enacted in 1988, for instance, while the NIGC MICS were not promulgated until 1999.

The California Horse Racing Board (Board) has detailed regulations as to the types of races, wagering, and pools, as well as requirements for outside audits to be performed and submitted to the Board. The California Lottery similarly has many regulations.

These above-noted regulations, from not only the Commission, but also from other State agencies are substantially more invasive from the viewpoint of the regulated entity than is CGCC-8. Indeed, CGCC-8 does not mandate NIGC MICS, or even State-adopted MICS, or in any way govern procedures in the Tribal Gaming Operation: that is the province of the TGA as the primary regulator. Rather it establishes a baseline for Compact compliance and provides protocols for interaction.

(iii) **Uniformity**. CGCC-8 encourages uniformity in many ways.

First, CGCC-8 encourages uniformity in Tribal Gaming in recognizing the NIGC MICS as the industry standard internal controls by adopting them as the "Standard of Compliance." The SGA will consider Tribes that adopt the NIGC MICS, or Tribal

[17] Title 4 CCR section 12402.

[18] Title 4 CCR section 12403.

[19] Title 4 CCR section 12403(a).

[20] Title 4 CCR section 12403(d).

MICS that exceed the NIGC MICS, to have adopted Compact compliant Tribal MICS. Some Tribes also have decided to adopt Tribal MICS which are not equal or more stringent than the NIGC MICS. These may nonetheless be Compact compliant, but further inspection and analysis would be necessary.

Additionally, some Tribes have also voluntarily submitted to the Federal government's "jurisdiction" via ordinance.[21] These Tribes again have adopted the NIGC MICS, and would be considered to have adopted Compact-compliant Tribal MICS. Additionally, all of these Tribal Gaming Operations would be subject to an independent agency's periodic comprehensive review/inspection of the Gaming Operation by the SGA or the NIGC, as well as a review of their Tribal MICS. The SGA would not directly inspect Compacted Tribes where the CGCC-8 section (m) Alternative Compliance section applies. Rather the SGA would review all the NIGC's reports, documents and workpapers papers it received from the Tribe as a result of the NIGC's comprehensive audit every three years, and then only investigate as necessary. However, all of these Tribes would be subject the same standards for what is considered Compact compliant Tribal MICS and valid enforcement of those Tribal MICS.

It should be noted that some Tribes in the past have asserted that the Commission's CGCC-8 does not "foster uniformity" because uniformity is accomplished by the Tribes voluntarily consenting to NIGC "jurisdiction and authority" in its entirety and the SGA should merely accept that without further review or conditions. However, that argument is problematic for two reasons. First, the provisions in the ordinances related to NIGC MICS are *voluntary* and can be cancelled or amended at any time. Second, after the *CRIT* decision, the NIGC's jurisdiction and authority under IGRA to regulate Class III gaming is suspect and possibly the subject of future litigation.[22] In addition, the validity of the NIGC's "exercise" of this monitoring and enforcement given to them by the Tribe through the ordinances is an open question; several tribes have challenged this NIGC policy. Moreover, it is significant that for six years, from 2000 to 2006, NIGC had completed on-site comprehensive compliance reviews for only eight California Tribes. At that rate, it would take **42.75 years** to complete NIGC MICS compliance review for all California gaming Tribes.[23] CGCC-8 thus is necessary.

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[21] Some Tribes have adopted regulations which are said to accomplish the same purpose as the ordinances. These are also voluntary and do not have the procedural burden of seeking NIGC approval.

[22] Some Tribes have intimated as much in comments received by the Commission.

[23] The 42.75 year estimate is based on the following. It took six years to complete eight audits, indicating it took .75 years to complete one audit. In California, there are 57 tribes operating casinos. If you multiply .75 times 57 tribes, the result is that it would take 42.75 years to complete audits of all 57 tribes. See also Written Remarks of National Indian Gaming Commission Chairman Montie R. Deer before the Senate Committee on Indian Affairs, March 14, 2002, in which he stated that "at current [NIGC] staffing levels, it would take twenty to thirty years for the Commission to evaluate each of the existing gaming operations." (See Exhibit "G" referenced above.)

However, without making any determinations or concessions as to the NIGC's authority to do this monitoring and enforcement, the Commission has decided to recognize this relationship via CGCC-8 the section (m) Alternative Compliance section. This encourages uniformity by allowing the SGA to review the workpapers of a comprehensive NIGC audit to ensure Compact compliance similar to how the SGA would itself perform a comprehensive Compact inspection of a Tribe that had no ordinance or regulation for NIGC review. This also encourages uniformity by the adoption of the NIGC MICS and decreases the burden on the Tribes at the same time. The SGA cannot accept anything less than a comprehensive NIGC audit with a review of the documents, as completely deferring to the NIGC would require a Compact amendment and an abrogation of SGA Compact authority.

Second, CGCC-8 encourages uniformity in the *process* of inspecting the Tribal Gaming Facility and Operation and provides a framework for interaction over the results of that inspection. The Compacts do not place any requirement that the SGA perform inspections on different Tribes in the same manner or even consider the NIGC MICS. A few examples of uniform standardization of the inspection process which otherwise are not required of the SGA include:

1) SGA notification in writing 30 days in advance of an inspection,
2) The SGA shall have an entrance interview/conference with the TGA,
3) The SGA will have an exit interview/conference,
4) The SGA will prepare draft report for the Tribe and TGA's review,
5) The SGA will interact with the TGA over a Tribal Action Plan,
6) The SGA and the TGA will be able to interact with Staff and the Commission (SGA) before a draft report is considered "Final."
7) The Final Report will include the Tribal response, if any.
8) Designation of one entity, the Commission, as the SGA to inspect Tribal MICS, rather than both the Commission and the Bureau of Gambling Control.

Without CGCC-8 there is no requirement that the SGA would have to proceed in this fashion at all, or even the same way from one Tribe to the next. Thus, this regulation is necessary for the uniformity it provides to the Compact inspection process.

(iv) **Alternatives**. An alternative to adopting the NIGC MICS as the "Standard of Compliance" would be to create a new set of minimum internal control standards. This would take a great deal of time and energy, and would result in Tribes having to re-test and perhaps change their internal control systems to make sure they were in compliance.

Another alternative would be outright mandating the adoption of the NIGC MICS. This was a part of a previous version of CGCC-8 which was voluntarily removed by the Commission in an effort to be more responsive to the Tribes, while still fulfilling its goal for encouraging uniform adoption of NIGC MICS post-*CRIT*.

A final alternative that has been suggested by some Tribes is for Tribes to enter into agreements with the Federal government to perform the oversight or to voluntarily submit to the Federal government's jurisdiction via ordinance without SGA inspection, review, and oversight of the NIGC's efforts. However, as explained above, that is not a viable alternative because consent could be withdrawn at anytime and the NIGC does not ensure Compact compliance: only TGAs and the SGA perform this role. Although the NIGC still has authority to approve Class III gaming ordinances (see 25 U.S.C. section 2710(d)(1) and (2)), the *CRIT* decision held that they had no authority to regulate Class III Gaming Operations. Their authority to enforce and review Gaming Operations under the ordinances is an open question that some Tribes still challenge. The decision to allow the NIGC to inspect is entirely voluntary. Thus, the problem with the ordinance approach is that a Tribe may subsequently amend the ordinance to remove the NIGC MICS provision and the NIGC Chairman might be unable to disapprove the ordinance on that ground. (See 25 U.S.C. section 2710 (d)(2)(B).).[24] As a result, the SGA has created the (m) Alternative Compliance section with requirements and limitations necessary for it to allow the SGA to fulfill its role under the Compacts while still allowing the Tribes the benefits of their relationship with the NIGC.

As noted above, it is significant that as of March 2007, NIGC had completed compliance reviews from 2000 to 2006 for only eight California Tribes.[25] The just recently published NIGC Strategic Plan (FY 2009-2014) notes on page six under Objective 1.1(Effectively monitor and enforce Indian gaming laws and regulations), that "operational compliance audits have resulted in hundreds of findings of non-compliance with required minimum internal controls relative to cash handling and revenue accountability."[26] Thus, there is a need for this CGCC-8 and the Alternative Compliance section including the requirements and limitations. The State completed all Five MICS reviews via MOUs[27] in the 2008/2009 fiscal year. Minimal or non-existent Federal oversight is not a substitute or alternative for effective oversight by the State through the Compact.

Some have also suggested that the NIGC be allowed to "design" an audit to ensure NIGC MICS compliance in lieu of a comprehensive audit and that the results and

[24] It has also been suggested that the State should enter into agreements with each Tribe. First, this is unnecessary because the SGA has the express authority through the Compact to adopt statewide regulations. Even if for some reason the State would want to do that, there is no guarantee of uniformity because different Tribes would want different standards. Finally, such agreements would require each Tribe to waive sovereign immunity.

[25] NIGC provides federal oversight to approximately 443 tribally-owned, operated, or licensed casinos operating in 29 states. Source: *NIGC Strategic Plan for Fiscal Years 2009-2014*, Overview, page one. (See Exhibit "F" referenced above.)

[26] See Exhibit "F."

[27] The three effective MOUs and one MOA with various tribes specifically provide that they are in place so long as the statewide uniform MICS regulations are not yet in effect. (There are four MOUs but one has not yet been signed by the Tribal Chair.)

documents of this should be provided. Such a "designed" audit could include a review of the Tribe's internal auditors and other documents, and where the NIGC obtains sufficient assurances of compliance no further inspection would be necessary. However, as discussed above, NIGC's inspection demands exceed their resources. Furthermore, even if these "designed" audits provide the NIGC assurances of NIGC MICS compliance, they do not provide the SGA with sufficient assurances related to its Compact compliance inspection rights. These include the review of Tribal contributions to the General Fund, Special Distribution Fund, and Revenue Sharing Trust Fund. NIGC MICS are interrelated with these inspections as they are adopted as Tribal MICS. Without access to a "comprehensive" report on Tribal MICS, including specific compliance exceptions, as well as all reports and workpapers, the SGA would be limited in following its Compact obligations. Such an action would require a Compact amendment.

(v) **Legal Authority**. See section above.

(vi) **If Statement of Need Identifies Factual Basis as the Rationale for the Need, Address Whether Duplicative**.[28] The Association's Task Force Report asserts that CGGC-8 duplicates a provision of the Indian Gaming Regulatory Act, 25 USC Section 2710(b)(2)(C) and the MICS portion of certain existing Tribal regulations.

The Task Force Report at page 2 criticizes CGCC-8 for mandating "external financial audits" which are already required by IGRA and by Compact section 8.1.8 and asserts there is no legitimate basis for including the financial audit provision. The current version of CGCC-8 omits the previous version's subsection (e) covering financial statements audit; hopefully eliminating the concern over duplication

The Task Force Report similarly suggests that CGCC-8 is duplicative because "a number of California gaming Tribes" have amended their Tribal gaming ordinances to incorporate the NIGC MICS and to grant the NIGC authority to enforce those standards. The Task Force Report argues that, since they have voluntarily submitted to NIGC jurisdiction and authority, CGCC-8 is duplicative. The Commission rejects this argument for five reasons, some of which were discussed above.

First, the NIGC MICS amendments to the ordinances are *voluntary* acts on the part of the Tribes. It is true that NIGC retains authority to approve Class III gaming ordinances, as explicitly stated in IGRA section 2710(d) (1) and (2). *CRIT* dealt with *regulation* of class III gaming operations; it did not eliminate all NIGC authority concerning Class III matters. The problem with the ordinance approach, however, is that a Tribe may subsequently amend its ordinance to remove the NIGC MICS provisions and the NIGC Chairman in all likelihood cannot disapprove the ordinance

[28] The Task Force objection on grounds of "duplicative" arises from the Protocol (B. 2(b) (vi)), which may have been inspired by the rulemaking part of the California Administrative Procedure Act (APA). According to Compact section 8.4, the rulemaking part of the APA does not apply to SGA uniform regulations. Under the APA, a proposed State agency regulation must satisfy the "non-duplication" standard (Government Code sections 11349.1 and 11349(f)). However, "non-duplication" is not one of the grounds that the parties to the Compact agreed could serve as a basis for an objection to a proposed regulation.

amendment on the ground that a Tribal ordinance must contain a NIGC MICS provision. See IGRA section 2710(d)(2)(B). That would clearly be a violation of the holding of CRIT.

Second, the NIGC does not have authority under IGRA to regulate Class III gaming operations; no agreement or Tribal ordinance can provide such regulatory authority. Additionally, the State's authority to regulate Class III Gaming Operations pursuant to IGRA is not secondary to that of the Federal government. IGRA states under section 2710(d)(1)(C) that Class III gaming activities of the Gaming Operation must be conducted "in conformance with a Tribal-State Compact." Here, the Compact gives the State the authority to inspect the Gaming Operation for compact compliance as well as provides the ability to adopt uniform regulations. Allowing the NIGC to supplant the SGA's Compact role via ordinance would be a violation of IGRA and the Compact as written.

Third, the NIGC does not verify Compact compliance and cannot according to IGRA and CRIT. That is the TGA and the SGA's role under the Compacts. Furthermore, compliance with Tribal MICS is interrelated with all other aspects of Compact compliance including the aspects that the Commission has been mandated to review by legislative enactment, executive order, and by the Compact. These specifically include the SDF, the RSTF, and General Fund audits. These areas are not the province of the NIGC.

Fourth, the Commission, despite these concerns, has attempted to respect these relationships after they have already been entered into by creating the Alternative Compliance section. As more thoroughly discussed elsewhere, this provision allows the NIGC to perform a comprehensive NIGC MICS review within three years with the SGA merely receiving the supporting workpapers and reports and asking investigate as necessary. This allows the SGA to verify Compact compliance without the Tribal Gaming Operation having multiple Governmental entities on site.

Fifth, pursuant to the Compact, provisions of uniform State regulations adopted under Compact section 8.4 are <u>binding</u> on the Tribes. Only a binding regulation can fully protect the public interest and not voluntary ordinances with no safeguards and requirements.

(vii) **Unnecessary**

The Task Force's and various Tribes "duplicative" comments may also be read as suggesting that CGCC-8 is "unnecessary." For the reasons noted above, we believe that the Task Force Report has not met its burden of persuasion on this issue, that is,

the Report has not demonstrated that CGCC-8 is "unnecessary" within the meaning of Compact section 8.4.1(e).[29]

Finally, we note that section 8.4.1(e) in addendum A, Modification No. 2 states:

"The Tribe may object to a State Gaming Agency regulation on the ground that it is unnecessary, unduly burdensome, conflicts with a published final regulation of the NIGC, or is unfairly discriminatory, and may seek repeal or amendment of the regulation through the dispute resolution process of Section 9.0; provided that, if the regulation of the State Gaming Agency conflicts with a final published regulation of the NIGC, the NIGC regulation shall govern pending conclusion of the dispute resolution process." (Emphasis added.)

This subsection indicates that conflict with a final published NIGC regulation was a matter of sufficient importance to the parties to warrant listing among the authorized grounds for objection to a proposed statewide uniform regulation. At the outset, CGCC-8 cannot conflict with a published NIGC regulation because the NIGC has been held to have no Class III regulatory authority. Additionally, by contrast, there is no mention of duplication in 8.4.1(e).

Further, while the Compact clearly states that a conflicting NIGC regulation is to govern pending conclusion of the dispute resolution process, one may logically infer that a readopted statewide uniform regulation which is allegedly unnecessary, unduly burdensome, or unduly discriminatory (or which allegedly has a flaw other than those matters specifically listed by the parties as grounds for objection) shall govern pending conclusion of the dispute resolution process.

7. FURTHER RESPONSE TO "COMPACT AMENDMENT" COMMENT

The Association's February 2008 Task Force Report asserts that the State does not have the power under Compact section 8.4 to supplement or interpret Compact provisions and that uniform statewide regulations are valid only if Tribes consent to them. If the State desires to address the topic of minimum internal control standards, the Association asserts that the State's only option is to seek Compact amendments.

The Commission believes that the Compact did not leave the State defenseless and paralyzed, that is, that the State has the ability under the Compact to ensure that the Tribes adhere to

[29] Under the California APA (expressly not applicable here pursuant to Compact section 8.4), the State Agency adopting a regulation must demonstrate by substantial evidence that the proposal is "reasonably necessary" to effectuate the purpose of the statute (Government Code sections 11340(c), 11342.2, 11349(a) and 11349.1(a)(1)). Here, by contrast, the burden is on the tribe to show that the uniform tribal regulation is "unnecessary." Compact section 8.4.1(e).

minimum standards consistent with the Compact and those formerly mandated by NIGC as industry standards and adopt regulations encouraging adoption of the NIGC MICS.[30]

In sharp contrast, a substantial number of the comments made in the February 2008 Task Force Report, and in Comments subsequently received from Tribes, though phrased in different ways, basically assert that the Compact does not authorize the SGA to adopt any regulation concerning internal control standards or NIGC MICS.

Indeed, one could reasonably conclude that the authors of the Report and Tribal comments believe that the SGA simply has no authority under the Compact to adopt regulations. This "nullity theory" essentially postulates that while it might appear on the surface that the Compact (section 8.0) expressly grants a substantial degree of rulemaking power to the SGA (subject to review in the dispute resolution process) for purpose of fostering "statewide uniformity of regulation of Class III gaming operations," on closer analysis, they assert, it becomes clear that the only option open to the State is to negotiate individual Compact amendments with each Tribe.

Though we respect this view, we assert that the proper procedure for any Tribe which rejects the State's role in developing uniform statewide regulations under section 8.0 would be to seek an amendment to its Compact deleting or revising section 8.0. For instance, the 2004 Coyote Valley compact and the 2007 Yurok Compact both have a regulations section (section 9), but this section does not authorize the SGA to adopt uniform statewide regulations. Rather, those two compacts provide a process whereby the SGA may adopt a Tribe-specific regulation.

Given the fundamental disagreement concerning the scope of SGA authority under the Compact to adopt a Tribal MICS regulation, and the underlying purpose of encouraging adoption of NIGC MICS post CRIT, as well as inspection protocols, CGCC staff has endeavored to ensure that CGCC-8 is drawn as narrowly as possible, while still assisting the TGA and Tribe in protecting the integrity of Tribal gaming.

8. CONCLUSION

In summary, CGCC-8 is an attempt to cooperatively encourage development and adoption of Compact compliant Tribal MICS and protocols for State inspection of Tribal Gaming Operations under the Compact in light of the *CRIT* decision giving rise to a greater need for State inspection

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[30] There are others who also agree with the Commission. For example, in a May 28, 2007 Copley News Service article by James P. Sweeney, "New Deals worth Billions to 5 Tribes," quotes tribal attorney George Forman as stating:

> "The state did not leave itself defenseless and paralyzed [under the 1999 Compact]."
>
> "[Forman] said the state has the ability under the compact 'to ensure that tribes adhere to (minimum standards) consistent with those mandated by the National Indian Gaming Commission.' "

This article is included as Exhibit "I."

and oversight under the Compact for Compact compliance. The adoption of the NIGC MICS as the "Standard of Compliance" under the "Safe Harbor" provision accomplishes a number of purposes, including using a standard with which Tribes have experience and are comfortable. It is also the industry practice which was created with substantial involvement by the Tribal community. Increased State oversight based on these clear protocols will accomplish a number of worthwhile goals. It will also give the State an independent basis for emphasizing publicly what has been an ongoing assumption: that many Tribal Gaming Operations are run with efficiency and integrity. Further, it will allow the State to better ensure protection of its citizens who frequent Tribal casinos and guarantee that the State's interest in the revenue sharing that is part of each compact is secure. Finally, it will allow the State to assist the Tribe and TGA in their Gaming Operation, while still respecting Tribal sovereignty.

PART II. ASSOCIATION'S OBJECTIONS

1. AUTHORITY TO PROMULGATE MICS REGULATION

Regarding the legal authority of CGCC-8, the Commission received comments from a number of Tribes. These comments contended that only a TGA is vested with the authority to promulgate and enforce rules and that the Association cannot displace a Tribe's sovereign governmental powers. Comments argued that there was no authority for CGCC-8 in the compact.

CGCC-8 is a regulation authorized under Compact section 8.4 to ensure uniformity in the regulation of matters encompassed by Compact sections 6.0, 7.0 and 8.0. It is an exercise of the SGA's authority under Compact sections 7.4, 7.4.4, 8.4 and 8.4.1.

It is clear under Compact section 8.4 that the SGA may promulgate regulations concerning matters encompassed by Sections 6.0, 7.0 and 8.0 in order to foster uniformity of regulation of Class III Gaming Operations throughout the State. Further, it is clear that notwithstanding that the Tribes have primary responsibility for administering and enforcing the Compact's regulatory requirements, the SGA has the right to inspect the Gaming Facility and Gaming Operation or Facility records and, notwithstanding any other provision of the Compact, the SGA is to be allowed access to papers, equipment and places where such access is reasonably necessary to ensure compliance with the Compact.

Compact section 7.4, provides the SGA the right to inspect the Gaming Facility and all Gaming Operation and Facility records related to Class III gaming activities. Furthermore, Compact section 7.4.4 makes clear the SGA's broad right of access to documents, equipment and facilities:

> "Notwithstanding any other provision of this Compact, the State Gaming Agency shall not be denied access to papers, books, records, equipment or places where such access is reasonably necessary to ensure compliance with this Compact."

See the Part 1 of this document, Section I.D., above, for further discussion of the State Gaming Agency's authority.

Some comments referred to the 2006 Compact amendments, contending that the existence of a NIGC MICS-related section in the amendments proved that the State is aware of the lack of authority to implement NIGC MICS under the 1999 Compact. The four Memoranda of Agreement and one Letter of Agreement have the following language:

> ***Section 104. Minimum Internal Control Standards (MICS).***
> ***Sec. 104.1*** *So long as the National Indian Gaming Commission does not have the authority to adopt, enforce, and audit minimum internal control standards (MICS) for class III gaming devices and facilities and the State Gaming Agency does not have regulations in effect that contain internal control standards that are no less stringent than those contained in the MICS of the National Indian Gaming Commission, the Tribe agrees to maintain in full force and effect and implement minimum internal control standards for class III gaming that are no less stringent than those contained in the Minimum Internal Control Standards of the National Indian Gaming Commission (25 C.F.R. 542), as they existed on October 19, 2006, and, during that period, to submit to enforcement and auditing by the State Gaming Agency to ensure that the Tribe is in compliance with such MICS. This section is intended to supplement the Amended Compact and is not intended to supersede or negate any provision of the Amended Compact or any regulation that may be adopted by the State Gaming Agency.*

These agreements contemplate that State regulations will contain MICS, but the agreements are merely an interim measure to keep the NIGC MICS as the standard until the State regulation (CGCC-8) is promulgated. There is no language indicating that this provision required additional authority be granted to the State. In fact section 104.1 specifically provides that:

> "[t]his section is intended to supplement the Amended Compact and is not intended to supersede or negate any provision of the Amended Compact or any regulation that may be adopted by the State gaming Agency."

Further, all Compacts have an express provision that makes clear that "neither the presence in another Tribal-State compact of language that is not included in this Compact, nor the absence in this Compact of language that is present in another Tribal-State compact shall be a factor in construing the terms of this Compact."[31]

Some comments asserted that the Commission had no authority to conduct a full financial audit. CGCC-8 never contemplated financial audits such as those found at 25 U.S.C. section 2710(b)(2)(C). However, in response to concerns raised by a number of Tribes, the current version of CGCC-8 has entirely omitted this section. It was certainly never the Commission's intent in CGCC-8 to purport that financial audits be conducted by the SGA.

[31] Compact Section 15.3.

2. NEED FOR REGULATION

Comments were received asserting that there was no need for the State to adopt a regulation setting minimum internal control standards. Since *CRIT*[32] validated what many Tribes had believed for years, that is, that the NIGC had no authority with regard to adopting regulations related to internal controls of Class III gaming, the legal landscape never changed and Tribes have been and continue to be self-regulating. The question has arisen as to what events have occurred which demonstrate that the State has a greater need for oversight.

The Commission believes that the *CRIT* court by deciding that NIGC did not have authority did not so much leave a "void" but rather clarified that Congress intended to leave Class III gaming regulation to the State and the Tribes, including independent, non-Tribal oversight of Class III Gaming Operations by the State. In response to widespread disagreement with that assertion and in response to language from various Tribes, the Commission has modified CGCC-8 throughout, including the purpose section of CGCC-8 (subsection (a)) to reflect the other aspects of the need and purpose of the regulation: to provide an effective and uniform manner in which the SGA can conduct inspections contemplated in Compact sections 7.4 through 7.4.4 and to encourage adoption of NIGC MICS as the "Standard of Compliance" for Compact Tribal MICS. Furthermore, the inspections include assuring Tribal (and TGA) compliance with the requirements of Compact sections 6.1, 7.1 and certain sections of 8.1 – 8.1.14, collectively the Tribal MICS.

The Commission agrees with the 2008 Task Force Report, and various Tribes' comments, that the *CRIT* decision does not and cannot change the terms of the Compact. However, we disagree with the proposition that CGCC-8 attempts to amend the terms of the Compact. For reasons expressed in more detail in the section on Legal Authority, Part 1, Section 4 above, we believe that the adoption of CGCC-8 is well within the Commission's authority, as provided in the Compact.

The Commission listened to the comments throughout the Association regulatory process and deleted references to *CRIT* in CGCC-8 because it became apparent that the citations themselves were unnecessary, although the regulation itself is nonetheless a valid exercise of authority under the Compacts. The Commission has also in subsequent meetings with Tribal representatives and attorneys, as well as during the Task Force's review of the April 15, 2009 draft, made substantial modifications to CGCC-8 to clear up any perceived ambiguity that appeared to expand SGA Compact authority.

Comments also stated that Tribes employ many persons as regulators and spend a great deal of money in self-regulation. The Commission respects these efforts, however that is not a reason for the SGA not to exercise its Compact compliance inspection authority given the interest in protecting the integrity of the Gaming Operation and the need to assure gaming is conducted

[32]See Part 1, Section 3 above for further discussion of the *CRIT* decision.

honesty and fairly. The TGAs and Tribes are also required to ensure Compact compliance under section 7.2.

In the cases in which a Tribe pays a flat fee[33] under the amended Compacts, the February 2008 Task Force report suggests that the State has no interest in securing its revenue share through the compliance reviews proposed in CGCC-8. There are, however, provisions of the NIGC MICS that are applicable even to a flat fee Tribe. Proper accountability of the number of machines in operation is essential. The NIGC MICS contain detailed processes, which in themselves cause an accounting of the number of machines operated.[34] Further, the NIGC MICS contain standards relative to information technology that protect the integrity of the data produced.[35] Another NIGC MICS section relates to the preservation of records, which is essential to validate the Tribe's assertion of machines operated.[36] These areas are all encompassed by the Compact required Tribal MICS. Additionally, all those Compacts implementing a flat fee system also contain unique Compact obligations relating to Gaming Devices in which NIGC MICS are invaluable for the Tribe to carrying out its obligations. In the broadest sense, the Tribal MICS and the "Standard of Compliance" NIGC MICS facilitate the credible operation of the Gaming Activity, which interest goes beyond the State's revenue share concerns, and is fundamental to the integrity of the entire Gaming Operation. (See also Section 6., "Unnecessary," below.)

Finally, some comments suggested that adopting the NIGC MICS by way of ordinance and providing for NIGC oversight eliminates the need for CGCC-8, the discussion of this is below. (See Part 1, Section 6, (iii and iv) above and 7, Duplicative, below, for further discussion of this suggested alternative.)

3. REGULATION OR COMPACT AMENDMENTS

Some comments argued that CGCC-8 was viewed as an unauthorized or premature renegotiation of the Compacts and that separate government-to-government negotiations should be undertaken pursuant to Section 12.0. Memoranda of Agreement were suggested as a separate negotiation.

From the Commission's perspective, Compact negotiations are not needed because the SGA's compliance inspection authority is clearly established in the existing Compact. While individual agreements could accomplish the same purpose, a uniform regulation adopted in accordance with the Compact provisions specifically authorizing such a regulation is much more efficacious. CGCC-8 encourages uniformity and fairness in SGA compliance inspections and, by taking into account the scope of individual Gaming Operations, based on the NIGC MICS assures a level playing field for all Tribes and prevents arbitrariness. Both the Tribe and the State are sovereigns. Each has sovereignty the other must respect; each has the right to demand that the

[33] There are only five such tribes.

[34] NIGC MICS, 25 CFR 542.13(h)(7), (10), (14) &(15); (m)

[35] 25 CFR 542.16(a), (b) & (f)

[36] 25 CFR5 42.19(k)

other sovereign comply with its responsibilities and obligations mutually agreed to in the Compact.

It was also suggested that CGCC-8 is inappropriately and unilaterally supplanting the TGA with the SGA and that, since MICS or NIGC MICS were not discussed in the Compacts, they cannot be added now.

CGCC-8 does not usurp the primary role of the TGA in establishing and enforcing Tribal MICS under Compact section 7.0. The current version of CGCC-8 does not mandate that the Tribe and TGA adopt the NIGC MICS. Rather it provides the NIGC MICS as the "Standard of Compliance" for Compact compliant Tribal MICS. If the NIGC MICS are adopted, the Tribe will have Compact compliant Tribal MICS. However, Tribes and TGAs can adopt something different but it will nonetheless be subject to further SGA inspection for Compact compliance. CGCC-8 also establishes guidelines and procedures for the SGA in exercising its authority under Sections 7.4 through 7.4.4 to independently ensure that the TGAs are carrying out their responsibilities under the Compact; in short, to ensure compliance with the Compact. Indeed, Compact Section 7.4 makes clear that notwithstanding the primary regulatory and enforcement role of the TGA, the SGA may inspect the Tribe's Gaming Facility and Gaming Operation or Gaming Facility records with regard to Class III gaming, subject to conditions outlined in Sections 7.4.1 through 7.4.3:

> "Notwithstanding that the Tribe has the primary responsibility to administer and enforce the regulatory requirements of this Compact, the State Gaming Agency shall have the right to inspect the Tribe's Gaming Facility with respect to Class III Gaming Activities only, and all Gaming Operation or Facility records relating thereto . . . "

The Compact provides the State with the authority, and indeed responsibility, to inspect Tribal MICS to ensure compliance with the Compact. The current version of CGCC-8 endeavors to remove any complained of ambiguity that could be perceived as a Compact amendment. Neither Tribal regulatory activities, nor NIGC regulatory activities can take the place of State Compact authorized compliance inspections. This would require a Compact amendment.

See also Part I. sections 4, Authority, and 6 (iv) (Alternatives).

4. "UNFAIRLY DISCRIMINATORY"

The Task Force Report and separate comments from Tribes indicate that because the State has not yet imposed MICS requirements in cardrooms, CGCC-8 is "unfairly discriminatory." See Part I, Section 6(ii), above, for a response to this comment.

5. "UNDULY BURDENSOME"

Comments from the Task Force Report and several Tribes indicate that CGCC-8 is "unduly burdensome." However, the adoption of the NIGC MICS as the "Standard of Compliance" would not pose a significant economic impact because TGAs have already adopted the NIGC

MICS and perform annual audits pursuant to IGRA. Revisions to CGCC-8 have been made to recognize the NIGC MICS in this fashion, and to generally streamline the process and lessen any impact.

The Commission reiterates that CGCC-8 has not and does not increase any obligation on the Tribes related to audits and inspections beyond that already provided for in Sections 6.0, 7.0, and 8.0 of the Compacts. Indeed, the current version of CGCC-8 attempts to lesson any perceived burden on the Tribe by including concepts such as the "Safe Harbor" and the "NIGC Alternative Compliance" section.

While any outside review necessarily entails the use of some Gaming Operation staff time and resources, the Commission is fully committed to working with individual TGAs through consultation on a case-by-case basis to conduct compliance inspections in the most efficient manner possible and therefore minimize any impact on Tribal Gaming Operations, TGAs, and California taxpayers. The Commission's ability to efficiently conduct meaningful compliance inspections depends to a large extent on the cooperation of individual TGAs and Gaming Operation personnel.

6. **"**UNNECESSARY"

Comments contended that CGCC-8 provides significant and unnecessary auditing by the Commission and that there has been no showing that Tribes are conducting gaming without standards to justify the implementation of CGCC-8. Further, for those Tribes that provide flat fee rather than percentages based upon net win, the State's interest in securing its revenue share through compliance reviews is lessened.

Even for those Tribes which provide a flat fee, the State has an interest in ensuring, through compliance inspections, that the TGA's regulations and internal controls protect the Gaming Operation from criminal involvement or corrupting influences and maintain fair and honest gaming by both the operator and players.[37],[38]

The NIGC has identified many instances of non-compliance in the limited number of NIGC MICS compliance reviews that they have conducted. See Part I, Section 6 (vi).

7. DUPLICATIVE

The Task Force Report and separate comments from individual Tribes argue that NIGC requires external auditing and if Tribes adopt ordinances containing NIGC enforcement of NIGC MICS, then CGCC-8 is "duplicative."

[37] Compact, Preamble, Paragraph A and Section 1(b).

[38] Even Tribes with flat fee payments revert back to the net win calculation after 18 years of lump sum payments to the State. The flat fee payments are based on so much per machine, and thus the number of machines is important, and the MICS provide a valuable tool for the State to verify the accuracy of the amount paid.

As has been made clear at the Task Force meetings and as Chairman Shelton made clear at the March 27, 2008 Commission meeting, the CGCC has and will continue to make every effort to coordinate with the NIGC. However, SGA compliance inspections are not duplicative of NIGC reviews; they are a legitimate exercise of the State's authority under the Compact.

As NIGC Chairman Philip Hogen's April 17, 2008 written testimony to the Senate Indian Affairs Committee Oversight Hearing stated:

> "To put the regulation of tribal gaming in proper context, we need to appreciate that the vast majority of the regulation of tribal gaming is done by the tribes themselves, with their tribal gaming commissions and regulatory authorities. In many instances, where tribes conduct Class III or casino gaming, state regulators also participate in the [regulatory] process. NIGC has a discrete role to play in this process and is only one partner in a team of regulators." (Emphasis added.)

The SGA focus is Compact compliance; the NIGC has no interest in, nor authority with regard to Compact compliance. Further, to assert that because the NIGC has an oversight role with regard to internal controls, the State should forbear from exercising its compliance inspection authority under the Compact is to ignore the State's role as a sovereign Compact signatory.

The Task Force Report points to Governor Schwarzenegger's letter of March 30, 2007 (attached as Exhibit "J") to the Senate Committee on Indian Affairs, quoting the governor as follows: "[California's] approach with the compacts and state oversight of internal controls has been to complement, rather than duplicate NIGC's activities."

CGCC-8 is not, as the Task Force Report asserts, "entirely inconsistent" with the Governor's message to the Senate Committee. In fact, it is not at all inconsistent. The fact that Tribes have already put into place standards "at least as stringent as NIGC MICS" does not make CGCC-8 duplicative. Nor does the fact that a number of Tribes have changed their gaming ordinances or entered into agreements purporting to grant the NIGC "authority" to monitor and enforce Tribal compliance with those standards. The loss of such authority as a result of the *CRIT* decision highlighted the need for the State to again exercise its Compact compliance oversight right. The authority for such oversight has always existed in the Compact -- it was just not exercised in its entirety or uniformly.

However, in the spirit of government to government relations, the Commission has sought to respect this relationship between the NIGC and the Tribe, by adopting the CGCC-8 section (m) Alternative Compliance section. This section serves to eliminate any perceived ambiguity about duplication under previous versions of CGCC-8 with the NIGC. This section requires certain strict procedures and protocols for it to be effective, including providing the SGA with the NIGC's workpapers and all reports related to the NIGC's comprehensive NIGC MICS review which must be conducted every three years. Possessing these documents and allowing the SGA to investigate where necessary allows the SGA to conduct its role of Compact compliance inspections by reviewing the documentation without needing to perform the Compliance

inspection onsite itself. Mandating anything less than these requirements would negate the SGA's Compact inspection right and authority. This would require a Compact amendment.

As indicated above, CGCC-8 no longer addresses financial audits, so there is no duplication of auditing or conflict with Sections 5.3(c) or (d) other than what is already required under Compact section 8.1.8.

As stated above, CGCC-8 does not duplicate TGA regulatory enforcement, as suggested by comments from the Task Force Report, and several Tribes. CGCC-8 merely informs as to what the SGA will consider to be Compact compliant Tribal MICS, and provide for protocols for Compact inspections. Any "duplication" of regulatory enforcement is ultimately under the requirements of Compact itself.

The Commission expects that the vast majority of gaming Tribes have standards in place and run their Gaming Operation according to those standards in compliance with the Compact. However, that does not alter the State's clear authority to conduct Compact compliance inspections. Further, from the perspective of the SGA, the State not only has the authority to conduct compliance inspections, but the responsibility as well. The public as well as the legislative and executive branches of State government have made that clear. CGCC-8 simply outlines a process and sets uniform benchmarks for such inspections. The State has not arrogated to itself any authority not already found in the Compact.

8. SPECIFIC REGULATORY LANGUAGE COMMENTS

Comments and responses to comments received after the October 14, 2008 Re-adoption of CGCC-8 can be found in the Accompanying Public Legal Memorandum.

9. ALTERNATIVES TO MICS REGULATION

Tribal Task Force members proposed alternative language that contemplated either waiting for new Federal authority for the NIGC or eliminating SGA compliance review via CGCC-8 if the Tribe and the NIGC agreed to NIGC oversight through either MOU/MOAs or changes to Tribal gaming ordinances. Neither of these approaches takes into account the State's sovereignty as a signatory to the Compact. The SGA authority to inspect the gaming facility and all gaming operation or facility records relating thereto (Section 7.4) and the SGA's authority to be granted access to papers, books, records, equipment or places where such access is reasonably necessary to ensure compliance with the Compact (Section 7.4.4) are derived from the Compact. They are not and cannot be made dependent upon the statutory authority of the NIGC, or upon other arrangements between the NIGC and individual Tribes as discussed above. The State's authority and Compact inspection obligation is not secondary to the Federal government's non-existent statutory authority over Class III Gaming Operations and the State is not obliged to delegate its authority to NIGC.

However, while respecting these concerns, the current version of CGCC-8 allows for the Alternative Compliance section with the NIGC review under certain strict conditions necessary

to protect the State's Compact rights are protected, while also decreasing the burden on TGAs and the Tribe regarding onsite inspection, and respecting their relationship with the NIGC.

10. "SAFE HARBOR" ALTERNATIVE THROUGH ASSOCIATION

Several Tribes assert that the State should reach statewide uniformity through cooperative action with the Association without mandating conduct or amending the compacts. The Tribes contend that an example of that is uniform regulation CGCC-2 related to registration of qualified bondholders, which did not mandate that it be followed, but provided that if followed, the Tribes and their bondholders would be deemed to be in compliance with the compact. One Tribe argues that this process, even though voluntary, provided complete assurance ("safe harbor") that preserved the regulatory integrity of those financings. However, the CGCC-2 example is not comparable to the CGCC-8 situation. First, CGCC-2 was agreed to because it substituted a process that was easier to accomplish than the more complicated requirements of the Compact. Although CGCC-2 does find that TGA shall be "deem[ed] to satisfy suitability standards of the Compact" if the applicant meets the requirements for registration under the regulation, it allows a more streamlined process for a determination of a Finding of Suitability for a Financial Source.

In contrast, CGCC-8 is not relaxing a Compact requirement. It is merely providing a framework for transparent and uniform interaction between the TGA, Tribe and the SGA. The current version of CGCC-8 attempts to incorporate the idea of a "Safe Harbor" to the extent possible by clearly stating that the "Standard of Compliance" for Compact compliant Tribal MICS are the NIGC MICS. TGAs may voluntarily choose to adopt or not adopt them, but they must still adopt Compact compliant Tribal MICS. CGCC-8 is ultimately very different than what occurred with CGCC-2. Further, although Findings of Suitability for Financial Sources are important, the process dealt with in CGCC-2 is not integral to the process of protecting the integrity of gaming. Under CGCC-8 the Tribal MICS are integral to gaming and cannot be voluntarily agreed to, with no ability on the part of the State to ensure Compact compliance.

11. RESPONSE TO (1) THE VOTE BY THE DEPARTMENT OF JUSTICE, BUREAU OF GAMBLING CONTROL AT THE SEPTEMBER 4, 2008 ASSOCIATION MEETING

At the September 4, 2008 meeting, the Department of Justice, Bureau of Gambling Control voted:

> "Yes to oppose the regulation CGCC-8 with the following comments:
>
> 1) We encourage tribes to consent to oversight; and
>
> 2) If the tribes are unwilling to consent, we would generally support the idea of the application of the federal standards without modifications." (Emphasis added.)[39]

[39]See the letter from Paskenta advocating this position, also included in the original Detailed Response attached as Exhibit E.

This Bureau comment is too vague to permit an effective response. In what form would the consent come, to whom would it be rendered, and in what kind of vehicle? How would it be enforceable and would the State need a waiver of sovereign immunity from each Tribe?

The BGC participated in discussions with Tribal attorneys and the Task Force review of the April 15, 2009 draft of CGCC-8 and the creation of the August 7, 2009 Task Force draft. The current draft recognizes the NIGC MICS as the "Standard of Compliance" and an industry standard. It also allows for the NIGC Alternative Compliance section with certain requirements and provisions to protect State Compact interest. It is unclear whether the Bureau still supports the statement made at the September 2008 meeting or whether the Bureau's view might be different based on the current version of CGCC-8.

12. RESPONSE TO ASSOCIATION AND TASK FORCE OBJECTIONS THAT TASK FORCE PROCESS AND AUGUST 6, 2009 VERSION OF CGCC-8 WAS IGNORED NOT CONSIDERED, AND THAT THE CGCC DID NOT ENGAGE IN THE PROCESS

The Commission vehemently disagrees with any assertion that the Task Force process and August 6, 2009 Draft of CGCC-8 was ignored and must be "reconsidered," as well as that that the CGCC was not "engaged" in the process or that the Task Force version was considered. The Commission greatly appreciated the Task Force process and the ability to actively dissect all aspects of CGCC-8 with the many TGA delegates and attorneys.

In contrast to the assertion that the process was "ignored" or that the Commission was not "engaged," Commission Staff participated in every Task Force meeting scheduled at the start of the process.[40] Commission Staff interacted on many interim drafts that it received from various Tribes, including some that were not received in advance making true meaningful dialogue difficult. Commission Staff attempted to explain the reasons why CGCC-8 contained provisions, and discussed how the precise wording was chosen. As the Task Force delegates are aware many of these discussions lasted for hours and included intensive debate and negotiation amongst Tribal delegates themselves and SGA delegates as well. Commission Staff also discussed how certain Task Force comments to alter various sections could be accepted, and also why certain comments would not likely garner support. The entire process was interactive and thorough. Thanks to this process, many improvements were made to the regulation.

Some Tribes also commented that Task Force version has not been endorsed. At the conclusion of the Task Force, it prepared another Report which included the Task Force's August 6, 2009 version of CGCC-8. The Report clearly stated that many, and not "all," the delegates approved this version. The Commission Staff present at the meetings could only remain neutral. Commission Staff does not determine policy or approve regulations at the Commission; Staff can only advise and make recommendations to the full Commission. Staff has reviewed the Task Force version, poring over the language and determining what it can recommend and what must

[40] In one instance, when a meeting was scheduled at the last minute, the Commission was unable to attend due to previously scheduled Commission meetings and to the press of other business brought on by the Governor's furlough orders.

be altered. This review and analysis is found here and in the accompanying summary and draft version of CGCC-8.

However, final decisions are always made by the Commissioners by a vote in open session as required by law. As a result, no final version of CGCC-8, including either the Task Force, or Staff's recommended version, or even other drafts subsequently received, have either been "endorsed" or "considered" by the Commission in any formal sense. These actions will take place, if at all, at the September 24, 2009 Commission meeting. In advance of this meeting Staff's recommended version of CGCC-8, this Response, and an accompanying Summary of the Process and Recommend Changes will be provided on line to all.