CALIFORNIA GAMBLING CONTROL COMMISSION

INITIAL STATEMENT OF REASONS

CGCC-GCA-2014-05-R

HEARING DATE: **November 5, 2014**

SUBJECT MATTER OF PROPOSED REGULATIONS: **Third-Party Providers of Proposition Player Services: Contracts**

SECTIONS AFFECTED: California Code of Regulations, Title 4, Division 18: **Sections 12200, 12200.7, 12200.9, 12200.10A, 12200.10B, 12200.10C, 12200.11, 12200.21, and 12560**

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).[1] Under the Act, the Commission is required to establish regulations under which the Bureau of Gambling Control (Bureau) may invalidate or prohibit an agreement or contract between a gambling enterprise and a third-party provider of proposition player services (TPPPS). Regulations concerning the procedures for the consideration and approval of contracts have been prepared to implement and make specific section 19984 of the Business and Professions Code.[2]

PROBLEM ADDRESSED:

Currently, Section 12200.7 provides the requirements for the contents of the TPPPS contracts. The TPPPS contract is currently required to include items best included as regulatory or compliance requirements, enforced by the Bureau, instead of contractual provisions enforced by the parties to the contract. Additionally, concerns have been raised that the regulations related to the determination of any contract payment amounts are not specific enough to ensure consistency with the regulation's original intent.

PURPOSE:

This proposed action has been prepared to implement and make specific section 19984 by clarifying the minimum elements that must be included in a TPPPS contract and clarifying which provisions are enforced by the Bureau. Additionally, the proposal provides specificity regarding how any payment by the TPPPS to the gambling enterprise can be determined in order to ensure

[1] Business and Professions Code, Division 8, Chapter 4, section 19800 et seq.
[2] All statutory references hereinafter are to the Business and Professions Code, unless otherwise specified.

that no payment allows the gambling enterprise to have any interest in the funds wagered, lost, or won.

ANTICIPATED BENEFITS OF PROPOSED REGULATION:

This proposed action will have the benefit of clarifying the TPPPS contract approval process by identifying how any payment by the TPPPS to the gambling enterprise shall be determined. Additionally, the proposed action will provide the Bureau with clearer criteria to use in reviewing and approving contracts, and ensures that the information required for review is clear and available. The gambling enterprise and TPPPS will benefit by having a clear understanding of what payments are allowed to ensure that their businesses are properly segregated and to help prevent illegal banking situations from occurring.

PROPOSED ACTION:

This proposed action will make changes within Article 1 of Chapter 2.1, and conforming changes in Chapter 10, Division 18, Title 4 of the California Code of Regulations.

The proposed changes in Chapter 2.1 are as follows:

Amend Section 12200. Definitions.

This proposed action would add three new terms to Section 12200, consolidate or delete several existing definitions and renumber various paragraphs accordingly. In addition, numerous grammatical, editorial and clarifying changes are made through the section.

Subsection (a) is modified to change the term "regulation" to "section." This is a minor grammatical or editorial change and has no regulatory effect.

Paragraph (1) of subsection (b) is revised to clarify to whom the additional badge is provided instead of just making a general reference to another section. This provides specificity to the definition, and is a minor technical editorial change without regulatory effect.

Paragraph (2) of subsection (b) is added to clarify the definition of "Affiliate." Section 19805, subdivision (a), provides a definition for "affiliate;" however, it does not provide clarity concerning which individuals or entities may fall under this definition. The proposed action provides for the additional use of "Affiliate of" and "person affiliated with," and provides clarity regarding the individuals and entities that are required to be reported by breaking down the different categories of control.

- Subparagraph (A) provides clarity for the types of individuals captured under the concept of control, as required by the Act. This subparagraph provides that individuals fall under this category if they are the spouse or registered domestic partner of the specified person.
- Subparagraph (B) provides clarity for the types of individuals captured under the concept of control, as required by the Act. This subparagraph provides that individuals fall under this category if they are another close family member of either

the specified person or the spouse or registered domestic partner of the specified person and either live in the same home as the specified person or participate in the management of any business in which the specified person has an ownership interest.

- Subparagraph (C) provides clarity for the types of trusts or other estates captured under the category of control. This subparagraph provides that trusts or other estates are considered under the control of the specified person or their spouse or registered domestic partner if either has a substantial beneficial interest or serves in a fiduciary capacity similar to that of trustee.
- Subparagraph (D) provides clarity for the types of businesses captured under the category of control. This subparagraph provides that businesses in which the specified person and their spouse or registered domestic partner own a combined interest of at least 10 percent are under the control of the specified person. The minimum 10 percent ownership interest threshold is intended to be consistent with the identification of specified persons and significant ownership.

It is necessary to identify those individuals and entities that are financially closest to individuals involved in the TPPPS contracting process. Section 19984 specifies that the gambling enterprise shall not have any interest in the funds wagered, lost, or won, and while the regulations have been crafted to ensure that inappropriate payments are not provided, the identification of these other sources allows for the process to ensure that inappropriate payments are not being provided through some other secondary avenue. In order to establish these secondary procedures, identification of the possible recipients of inappropriate funds is needed and the language of section 19805, subdivision (a) does not provide the specificity necessary.

Paragraph (3) of subsection (b) is revised to clarify that an applicant is a person applying for a registration or license. This is a grammatical, editorial clarifying change and it has no regulatory effect.

Paragraph (4) of subsection (b) is revised to be consistent with other changes. The language is changed to provide that it is the registration or license that authorizes play in a controlled game and not the badge. The final sentence, which is a control provision and not part of a definition, has been moved and incorporated into subsection (b) of Section 12200.21.

Paragraph (6) of subsection (b) is added to provide a definition for the term “derivative party.” This definition establishes a general term that may be used when referring collectively to the various owners of either a TPPPS or gambling enterprise. This definition is necessary so that a simple method is available to identify and refer to a TPPPS or gambling enterprise’s ownership.

Paragraph (7) of subsection (b) includes a non-substantive grammatical, editorial change that reorganizes an existing provision and that has no regulatory effect.

Subparagraphs (C) and (D) of paragraph (8) of subsection (b) are removed from the definition of “license” as they are not part of a definition. Subparagraph (C) has been moved

to paragraph (2) of subsection (b) of Section 12200.21 while subparagraph (D) is repealed as its provision is duplicative of paragraph (1) of subsection (b) of Section 12200.21.

Paragraph (10) of subsection (b) includes a non-substantive grammatical, editorial change that repeals an unnecessary internal reference and has no regulatory effect.

Paragraph (12) of subsection (b) is revised both to correct for a change in law and to move a definition to another location without change. The change to subparagraph (A) moves the definition of primary owner to paragraph (14), which is the actual definition of primary owner. Prior to this change, the definition of primary owner was only a reference back to subparagraph (A) of paragraph (12). Subparagraph (A) now uses the term primary owner for simplicity and clarity. The change to paragraph (B) is likewise non-substantive. In 2009, Assembly Bill (AB) 293 (Mendoza, Chapter 233, Statues of 2009) added new subdivision (f) which shifted the former subdivision (h) to subdivision (i). This proposed change simply conforms to the statutory change made by AB 293.

Paragraph (13) of subsection (b) includes a non-substantive grammatical, editorial change that clarifies and conforms to the definition of "proposition player" in paragraph (15), and has no regulatory effect.

Paragraph (14) of subsection (b) includes a non-substantive grammatical, editorial change that provides clarity to the definition of primary owner. Currently, the definition of primary owner is not actually provided under primary owner but instead as part of the definition of owner. This change directly links primary owner with its definition and has no regulatory effect.

Paragraph (16) of subsection (b) is amended to clarify that the proposition player contract is between the gambling enterprise and the primary owner of the TPPPS. The removal of the independent contractor reference removes an unnecessary and inaccurate description of the two-party relationship.

Paragraph (17) of subsection (b) is amended to clarify that a rebate may include a complete return of chips or money and is not limited to only a partial return. This change is necessary to clarify that a full return of chips or money is subject to all provisions related to rebates.

Paragraph (19) of subsection (b) contains non-substantive grammatical, editorial changes that bring the wording and formatting into conformance with the similar definition in paragraph (8). Additionally, subparagraph (C) of paragraph (19) is removed from the definition of "registration" as its provisions are not part of a definition. The first sentence of this subparagraph is now addressed in paragraph (2) of subsection (b) of Section 12200.21, while the second sentence is duplicative of paragraph (1) of subsection (b) of Section 12200.21. Therefore, subparagraph (C) should be deleted.

Paragraph (20) of subsection (b) includes a non-substantive grammatical, editorial change that deletes an unnecessary internal cross reference. Additionally, the definition is revised to

refer to a *proposition* player instead of player for clarity. The two terms have the same meaning under this Chapter. These changes have no regulatory effect.

Paragraph (21) of subsection (b) includes a non-substantive grammatical, editorial change that deletes an unnecessary internal cross reference and has no regulatory effect.

Paragraph (22) of subsection (b) is added to include a definition for "specified person." Section 19805, subdivision (a), provides a definition of affiliate. As part of this definition, individuals (the affiliates) are identified based on their relationship (control) with a specified person. The statutory provision does not provide any context or explanation of who is a specified person and this definition is proposed to do so. A specified person would be identified in relationship to a gambling enterprise, TPPPS, or gambling business based on an ownership interest of at least 10 percent. The definition of specified person is first limited to a consideration of owners of a business based upon the context of the Act. The purpose of the Act is to provide assurance to the public that gambling is safe and free from criminal influence. To accomplish this, individuals apply for and receive licenses, registrations, or some other form of approval. To receive this approval, applicants must undergo background checks. At the highest level are those applicants with direct control over the workings and assets of the business. It is from these people that the most damage can be done, and it is therefore to these people, and to those who can influence them, that the State has the highest level of interest. Many business structures do not include a single primary owner, but can include a multitude of individuals and entities, some with very small ownership percentages. Individuals with small ownership interests, even if influenced by others, may not be in a position to actually effectuate any action within the business. Therefore an exception to ownership is provided to remove individuals without this control, defined as someone with less than 10 percent ownership interest and no other reason of licensure (such as working in the facility). The value of 10 percent interest is consistent with the U.S. Securities and Exchange Commission's idea of beneficial ownership [United States Code, Title 15, Chapter 2B, 78p(a)].

Paragraph (23) of subsection (b) is revised to refer to *proposition* player instead of player for clarity. The two terms have the same meaning under this Chapter. This is a non-substantive grammatical, editorial change that has no regulatory effect.

Paragraph (24) of subsection (b) includes non-substantive grammatical, editorial changes that delete unnecessary internal cross references. Additionally, the definition is revised to refer to *proposition* player instead of player for clarity. The two terms have the same meaning under this Chapter. These changes have no regulatory effect.

Paragraph (25) of subsection (b) is modified for consistency. The party to the contract is the gambling enterprise, specifically, and not the *house*, as defined in section 19805, and this change makes the definition reflect that difference.

Paragraph (26) of subsection (b) is changed from the definition "TPP" or "third party proposition" to "TPPPS" or "third-party provider of proposition player services." This is a

non-substantive grammatical, editorial change and brings the terms used in the regulations closer to the actual terminology used in the industry. In addition there is the non-substantive deletion of extraneous language. These changes have no regulatory effect.

Paragraph (27) of subsection (b) is revised to provide clarity as to whom the transfer badge is provided instead of just a general cross reference to another section. This provides specificity to the definition. This is a non-substantive grammatical, editorial change and has no regulatory effect.

Amend Section 12200.7. Proposition Player Contract Criteria.

This proposed action describes the minimum requirements of any contract between a TPPPS and a gambling enterprise, including; provisions that must be included in the contract, and how any payment under the contract can be determined. By providing these guidelines, the regulations help to ensure that there is a proper separation between the gambling enterprise and the funds waged, lost, or won during the play of controlled games.

Subsection (a) provides that even during the effective term of a contract, should the contract have any provisions that come into conflict with any changes in the Act; the contract is superseded by the statutory changes. The language is revised to expand the Act's application from just section 19984 to the entire Act. This helps to ensure that the contracts remain in compliance with the law if any relevant provisions of the Act are changed, not just section 19984. Additionally, the requirement that the contract be superseded by changes in the regulations is deleted and replaced with a provision in Section 12200.10 which would prevent an expedited review in the event that regulations have been revised. This allows these, and any other changes to the contract regulations to be adopted within the next contract cycle without requiring every single contract to be redone upon the effective date of these regulations as that would be burdensome to both the Bureau and industry.

Subsection (b) specifies the provisions that must be included in every contract. This subsection is revised with a non-substantive grammatical, editorial rewording. Additionally, the paragraphs contained within this subsection have been revised and renumbered as required.

Paragraph (1) of subsection (b) provides that the parties to the contract must be specified in the contract. Additionally, the requirement to provide both derivative parties and affiliates of the specified persons has been included. Other aspects of the contract process have been proposed to reference both of these categories of individuals. The necessity of those additional provisions will be provided in those sections. In order to provide a reference to these individuals, they must be identified. By identifying them in the contract, instead of just with the contract, other aspects of the processes would require that, should this list of individuals change during the term of the contract, notification to the Bureau would be required. Notification would provide the Bureau with the opportunity to reexamine the relevant parts of the contract to ensure continued compliance with the Act and regulations.

Paragraph (3) of subsection (b) provides that the specific name of any games that the TPPPS is providing services for must be included in the contract. This paragraph has been revised to require the game number assigned by the Bureau in addition to the game name. The Bureau approves many games, and does not require that a specific name be linked to a specific set of rules, so often each cardroom will put a different spin on the game name. It is therefore possible that the same game number is given multiple names. Therefore, just providing the name does not actually identify a unique game. By providing the game number, a unique game is identified.

Additionally, the reference to gaming activities is changed to controlled game(s). The term "gaming activity" is defined in Title 11, CCR, Section 2010, subsection (f); however, that is not the way this term is being utilized in this paragraph. The purpose of this paragraph is to identify the services being provided, not just jackpots and promotions as provided in the definition of "gaming activity." Therefore, for the purposes of clarity, the use of "controlled games," as defined in Business and Professions Code section 19805, subdivision (g), is utilized.

Paragraph (4) of subsection (b) specifies that the minimum and maximum number of tables available for service by the TPPPS must be provided. This section includes non-substantive grammatical, editorial changes to make the paragraph consistent with the terms used in this chapter. These changes have no regulatory effect.

Paragraph (5) of subsection (b) specifies that no more than one of any license type may simultaneously play at one table. This provision is moved to paragraph (4) of subsection (b) of Section 12200.21. This provision is not a contractual issue, but instead a compliance standard that should be enforced by the Bureau and not the parties to the contract. By moving it to Section 12200.21, the provision becomes clearly enforceable by the Bureau. A new paragraph (5) would specify that if there is an agreement to prohibit any other TPPPS or a gambling business from operating in the gambling establishment, it must be included in the contract. This is a non-substantive grammatical, editorial change as subsection (a) of Section 12200.21 already contains this provision. Section 12200.21 is not the most appropriate regulation in which to include this provision, and it has been incorporated into the section specifically intended for detailing contract terms.

A new paragraph (6) of subsection (b) is added and the current paragraph (6) is renumbered as paragraph (7) accordingly. The new paragraph (6) requires that if the TPPPS is to be assigned a dedicated seat at a table it must be specified in the contract. This is a non-substantive grammatical, editorial change as subsection (a) of Section 12200.21 already contains this provision. Section 12200.21 is not the most appropriate regulation in which to include this provision, and it has been incorporated into the section specifically intended for detailing contract provisions.

The current paragraph (7) of subsection (b), renumbered as paragraph (8), requires that if specific items are being stored by the TPPPS at the gambling establishment, the purpose of those items must be included in the contract. Additionally, the location and security

measures for the space must be included. A requirement to also include the location of the storage facilities utilized by the TPPPS within the gambling establishment is added to this paragraph. By including this information, the Bureau is made aware of what facilities are being provided by the gambling enterprise to the TPPPS in order to assess any link between facilities and payments. By specifying the purpose of the items being stored, the Bureau can not only assess the link between payments and facilities, but also the reasonableness of the payment amount.

Paragraph (8) of subsection (b) in the current regulation is repealed. This provision requires that the contract include a provision requiring compliance with laws and regulations pertaining to controlled gambling. By including this provision, it requires the parties to the contract (the TPPPS or gambling enterprise) to make judgment upon any possible violation of law and enforce it as a violation of the contract. Possible violations of laws or regulations should not be enforced through the contract, but should instead be reported to the Bureau for proper investigation and possible action through other regulatory processes. While this change would in no way remove the requirement that a TPPPS or gambling enterprise operate in compliance with the laws and regulations pertaining to controlled gambling, a provision is being added to Section 12200.21, as subsection (i), making it clear that the gambling enterprise is responsible for ensuring that proposition player services are conducted lawfully in their establishments.

Paragraph (9) of subsection (b) in the current regulation is repealed. This paragraph requires that the contract contain a provision that services may only be provided by authorized players who are licensed or registered. This requirement, while important, is not necessary in the contract. Requirements already exist that limit play to only authorized players, such as paragraph (1) of subsection (b) of Section 12200.21. Including it in the contract only authorizes the gambling enterprise to report a violation of a contract provision. Therefore, similar to other provisions, this change would instead put the focus on the Bureau's investigatory powers and not as a contractual issue between the parties.

Paragraph (10) of subsection (b) in the current regulation is repealed. This provision requires that the TPPPS must provide a copy of its registration or license to the gambling enterprise who shall maintain it on file along with a copy of the approved contract. While the two parties might desire such an exchange, there is no need for this to be required in the contract. The two parties should be allowed to maintain their business records as they mutually agree, with the Commission and Bureau already having separate access to all of these documents. The repeal of this provision would not prevent any local agency from requiring these documents be available and would not prohibit the contracting parties from voluntarily including a similar requirement in a contract.

Paragraph (11) of subsection (b) in the current regulation is repealed and moved to paragraph (3) of subsection (b) of Section 12200.21. This provision prohibits an individual who possess duel licensure (TPPPS and gambling establishment) from performing any TPPPS functions within their associated gambling establishment. This provision is critical, but

should not be enforced by the two parties through the contract, but instead by the Bureau. Therefore, this provision is moved to paragraph (3) of subsection (b) of Section 12200.21.

Paragraph (12) of subsection (b) in the current regulation is repealed and moved to subsection (c) of Section 12200.21. This provision clarifies that the TPPPS is required to pay the collection fees related to their level of participation at any stage of play. This provision is critical, but should not be enforced by the two parties through the contract, but instead by the Bureau. Additionally, the language is revised to provide additional clarity. The original language of "… as those charged to other participants during the play of the game" is unclear when the practicalities of rotation and collection fee schedules are taken into consideration. The original language could be interpreted to mean that at any given time two players have paid the same amount in collection fees. This is inaccurate, as during the play of the game collections fees can vary based on the amount being wagered. Additionally, the positions of player and player-dealer are generally not required to pay the same amount and players have an option of declining their turn to play. Therefore, to clarify the purpose of this provision, the language is revised to require that the amount paid must be the same "for the same level of participation" which will reflect the variations between positions and amounts wagered.

Paragraph (13) of subsection (b) in the current regulation is repealed. This provision requires that a copy of the playing book form be included as part of the contract. This provision only requires that the gambling enterprise approve, as part of the contract, the playing book form as the playing book form is already separately required to be submitted as part of the contract approval process of Section 12200.9. There is no reason for the playing book form to be agreed to by the gambling enterprise, and therefore this provision is not necessary.

Paragraph (14), renumbered as paragraph (9), of subsection (b) requires that any agreement related to the TPPPS inspecting or receiving copies of surveillance recordings be included in the contract. This provision is amended to change the term house to gambling enterprise. This change maintains consistency with other changes and clarifies that the contract is with the gambling enterprise and not the house. Section 19805 defines "house" as "…the gambling enterprise, and any owner, shareholder, partner, key employee, or landlord thereof." In the context of identifying the parties to the contract, the house is not the appropriate entity to fill that role. A key employee is just an employee of the business and while that person may be authorized to act in specific roles on behalf of the business, they are not a party to the contract or responsible for fulfilling the contract. Conversely, gambling enterprise, also defined in section 19805, means "…a natural person or an entity… that conducts a gambling operation…" As the party conducting the business, gambling enterprise is the more specific and relevant term to use to refer to a party to the contract.

Paragraph (15) of subsection (b) in the current regulation requires disclosure of any financial arrangements between the parties to the contract that may exist in addition to the specific provisions of the contract. This provision requires that any other arrangements be considered as part of the contract. This requirement, while important, should not be an issue within the contract. The Bureau has a need for the information during the contract review, in order to have a complete understanding of the financial arrangements between the parties. This

allows the Bureau to ensure that the provisions of law and regulation related to the payment of funds are not being circumvented. This contract requirement is duplicative of other similar provisions and is therefore repealed. Whether the contract includes this provision or not the parties are still required to follow the requirements of the regulations. Proposed paragraph (8) of subsection (a) of Section 12200.9 includes the requirement that all financial arrangements must be reported with the contract; the new Section 12200.11 contains the requirements for modifying and amending a contract; and, a new subsection (j) in Section 12200.21 specifies how any new arrangements during the term of the contract must be reported to the Bureau.

Paragraph (16) of subsection (b) in the current regulation requires that any legal dispute between the parties to the contract be reported to the Bureau and Commission. While an important requirement, it is not one that must be required to be included in the contract. Accordingly, this provision is moved to subsection (d) of Section 12200.21 with only minor grammatical, editorial changes that have no regulatory effect.

Paragraph (17) of subsection (b) in the current regulation requires that any occurrence of a registrant being arrested or removed from the gambling establishment must be reported to the Bureau and the Commission. While an important requirement, it is not one that must be required to be included in the contract. Accordingly, the provision is moved to subsection (e) of Section 12200.21 with only minor grammatical, editorial changes that have no regulatory effect.

Paragraph (18) of subsection (b) in the current regulation requires that any occurrence of cheating reported to the gambling enterprise by the TPPPS must be reported to the Bureau and the Commission, in writing, within 5 days. While an important requirement, it is not one that must be required to be included in the contract. Accordingly, this provision is moved to subsection (f) of Section 12200.21 with only minor grammatical, editorial changes that have no regulatory effect.

Paragraph (19) of subsection (b) in the current regulation requires that if the TPPPS is allowed to provide rebates, any criteria must be provided for in the contract or, if rebates are not allowed, a statement to that effect must be included. This provision is deleted. Consistent with the proposed addition of subsection (k) of Section 12200.21, which would bar the TPPPS from issuing rebates, this provision is no longer appropriate or necessary.

Paragraph (20) of subsection (b), renumbered as paragraph (10), requires that if the TPPPS and gambling enterprise have a pre-arranged tipping agreement through which the TPPPS tips the gambling enterprise employees, it must be included in the contract. Additionally, if there is no agreement, a statement to that effect must be included in the contract. This provision is revised for clarity. Current practice includes the parties agreeing that tipping is allowed but not specifying a specific tip schedule, called “at discretion.” There has been confusion as to whether this qualifies as a tipping arrangement that must be included in the contract. The change provides this clarity by limiting the requirement to a yes/no response concerning tipping. The current provision requires that the specifics of the tipping

arrangement be included in the contract and while the change to this provision removes that requirement, the addition of subsection (g) to Section 12200.21 addresses tipping and tipping arrangements.

Paragraph (21) of subsection (b) in the current regulation specifies that any reimbursement by the TPPPS to the gambling enterprise for equipment must be included in the contract. This provision, while important, deals with the direct payment by the TPPPS to the gambling enterprise. Subsection (c) of this section is where payments are discussed, and therefore paragraph (21) is repealed and the requirement incorporated into the changes to subsection (c).

Paragraph (22) of subsection (b) in the current regulation requires that the contract include a provision that states the contract is a complete expression of all agreements and financial arrangements between the TPPPS and gambling enterprise and that any revisions must be approved by the Bureau in accordance with Commission regulations. This contract requirement is duplicative of other similar provisions and is therefore repealed. Whether the contract includes this provision or not the parties are still required to follow the requirements of the regulations. Proposed paragraph (8) of subsection (a) of Section 12200.9 includes the requirement that all financial arrangements must be reported with the contract; proposed Section 12200.11 contains the requirements for modifying and amending a contract; and, a new subsection (j) in Section 12200.21 specifies how any new arrangements during the term of the contract must be reported to the Bureau.

Subsection (c) in the current regulation provides the structure within which any payment to the gambling enterprise is determined. This includes limiting reimbursement to just services, facilities and advertising, and prohibiting the amounts from being based upon a percentage of the TPPPS's profits, wagers, or number of players and from being substantially disproportionate to the value of the services or facilities provided. This section is amended to improve the clarity of the payment restrictions and to remove unnecessary language.

Current subsection (c) contains only associated paragraphs and no direct provisions. The second and third sentences of paragraph (1) are moved to subsection (c). Together, these provide clarity that the contract must include all direct payments between the TPPPS and the gambling enterprise.

The first sentence of paragraph (1) of subsection (c) in the current regulation provides that payments may not be based on the profits or revenues of the TPPPS, unless expressly authorized. While this restriction is important, and is replaced by a similar provision, the qualification of "[e]xcept as expressly authorized…" has no meaning as there is no exception included in the current, or amended regulations. This restriction is maintained as paragraph (1) but modified to more closely meet the restriction provided for in section 19984 as restricting interest in the funds wagered, lost or won. The first half of paragraph (2) is then incorporated with the clarification that the gambling enterprise cannot receive money based upon a percentage of the TPPPS's profits and wagers. These modifications provide a

limitation to reimbursement more closely aligned with the Act, and provide a clear separation between the banking of a game and the offering of a game.

The last sentence of the current paragraph (1) requires that a detailed list, excluding specific costs, be included in the contract. This provision is modified and renumbered as paragraph (2) of subsection (c) to require a detailed list of all items provided for in the contract. The limitation of excluding specific costs is removed. The Bureau expressed concern that the restriction was making it hard for a review to be conducted to ensure that payment was consistent with the other requirements. It is a requirement of section 19984 to prohibit the connection of the gambling enterprise with the results of the play of a controlled game and, to ensure this, an analysis of the contract must be done. Restricting the information provided to the Bureau limits their ability to ensure compliance.

The current paragraph (1) also includes a restriction of payment to three categories: services, facilities and advertising. Additionally, the last sentence of the current paragraph (2) limits the payment to a fixed amount for the services and facilities and to a reasonable share of advertising. Finally, the first sentence of the current paragraph (3) disallows payments for services and facilities that are substantially disproportionate to their value. These three provisions provide an unclear limitation of the payment amount, using undefined concepts of value, substantially disproportionate and reasonable. The new paragraphs (3) and (4) clarify the restrictions.

A new paragraph (3) limits payments for services and facilities to their established value. Services and facilities are items with a more abstract expense associated with them. There will likely not be a purchase order or receipt to show the cost. While value is a concept currently in use, clarity is provided through the contract approval process where the TPPPS is required to provide, to the Bureau's satisfaction, a methodology that determines the value of each service and facility in order to show how that the payment was arrived at and that it is not excessive or disproportionate. Services and facilities provided to the public for free are not allowed as their value has been set at zero cost.

A new paragraph (4) relocates the provisions moved from paragraph (21) of subsection (b) of the current regulation and limits payments for advertising and equipment, to a proportionate share of the actual costs of each item that is directly related to the benefit to the TPPPS. The costs of advertising and equipment are known costs and therefore do not require the use of any methodology to establish their value; only the TPPPS' proportionate share. Accordingly, the application review process is modified to include substantiation of these costs.

Through, the new paragraphs (3) and (4), any TPPPS payment is limited to the costs generated by the TPPPS (services and facilities provided by the gambling enterprise to the TPPPS), and acknowledges the mutual interest in promoting and maintaining the game (advertising and equipment), but do not connect the gambling enterprise to the results of a controlled game.

Subsection (d) of the current regulation imposes a restriction preventing the parties from agreeing to any limitation on communications with the Bureau and the Commission, or taking any retaliatory action should those communications occur. This is changed to expand the agencies that are covered by this restriction beyond just the Bureau and Commission to include other licensing and law enforcement agencies. It is of paramount importance that any licensed party be able to communicate with any licensing or law enforcement agency without restriction or fear of retaliation.

Subsections (e) and (g) are consistently amended to clarify that a gambling *enterprise*, not a gambling *establishment*, is a party to the contract. These are minor technical, grammatical, conforming changes that have no regulator effect.

Amend Section 12200.9. Review and Approval of Initial and Renewal Proposition Player Contracts.

This proposed action modifies and clarifies those processes and procedures the Bureau must follow when reviewing and approving a contract. Additionally, this section is expanded to include the requirements for the renewal of a contract which limits duplicative language in the chapter.

Paragraph (1) of subsection (a) in the current regulation provides that the TPPPS may not perform services for a gambling enterprise until after a contract has been approved by the Bureau, and that to perform services without approval is a violation. Additionally, this subsection provides a list of conditions that must be met. The last sentence is amended to clarify that the conditions listed must all be met before a contract can be approved or renewed.

- Subparagraphs (B), (C) and (D) of the current paragraph (1) are moved to a new paragraph (2).
- New subparagraph (B) clarifies that the TPPPS must have a valid license or registration before a contract can be approved. This ensures that only authorized persons are applying for approval of contracts to offer third-party services, and streamlines the Bureau's review processes as they are not required to review a TPPPS contract unless those services could actually be provided.
- A new subparagraph (C) is added which works in conjunction with the new paragraph (3) of subsection (c) of Section 12200.7, by requiring that the values for services and facilities determined and provided for in the contract are not higher than their justified value. Additionally, the incorporated form BGC-APP-030 is modified to reflect the changes to the regulations and to incorporate the non-duplicative information of form BGC-APP-031, with that form being repealed.
- A new subparagraph (D) is added which works in conjunction with paragraph (4) of subsection (c) of Section 12200.7, by requiring that the documentation provided to substantiate payments or reimbursements for advertising or equipment do not exceed a proportionate share of the actual costs related to the benefit received by the TPPPS.

- A new proposed subparagraph (E) is added to move the provision from subsection (c) that limits the term of a contract to a two-year period. Moving this provision simplifies the number of places in the regulations that include limitations to the Bureau's approval of the contract.

Paragraph (2) of subsection (a) in the current regulation is repealed as it is redundant. This paragraph just introduces and requires that a specific form be submitted. This is redundant to the current paragraph (3) which requires that the same form be submitted as part of a complete application. As previously noted, a new paragraph (2) would provide a list of items that a contract cannot include. As noted, the new subparagraphs (A), (B) and (C) correspond to the relocated subparagraphs (B), (C) and (D) from paragraph (1) with only minor non-substantive grammatical, editorial changes that have no regulatory effect. Additionally, two options are included:

- Option 1 would provide two restrictions that would instruct the Bureau to not approve a contract if approving that contract would allow specific situations to exist.
    - The first situation [new subparagraph (D)] is where an owner of a TPPPS contracts for third-party services with an owner of a cardroom and each owner already has an approved contract. In this contract the owner of the TPPPS represents the cardroom in the other contract and the owner of the cardroom represents the TPPPS in the other contract.
    - The second situation [new subparagraph (E)] is where an owner of a TPPPS contracts for third-party services with an owner of a cardroom, and the two owners are also both owners in common of another TPPPS company, gambling business or gambling enterprise. The regulations, current and proposed, attempt to create a structure consistent with section 19984, which requires separation of the interests of a gambling enterprise from the play of a controlled game. The existence of a direct financial or controlling interest in a licensed business does not create an environment where the two parties can independently determine the value of a third-party contract.
- Option 2 would only provide for the prohibition of the second situation [new subparagraph (D)].

Paragraph (3) of subsection (a) in the current regulation is renumbered as subsection (b) and provides a list of the items that must be provided to the Bureau, along with the contract, in applying for initial approval. In addition, the incorporation of the contract approval application form (BGC-APP-030) is moved to this paragraph, as a result of repeal of paragraph (2) of subsection (a) in the current regulation.

- Subparagraph (B) of paragraph (3) in the current regulation requires the submittal of an Appointment of Designated Agent form (BGC-APP-031). This provision is repealed, as that form is being merged with the contract approval application form (BGC-APP-030) and will no longer exist.
- A new paragraph (6) is added which will work in conjunction with the new paragraph (3) of subsection (c) of Section 12200.7 by requiring that a methodology be submitted

that shows how the value of any services and facilities being provided in the contract were determined. It is outside the Bureau's scope of expertise to determine the local costs of rent, cleaning services or the multitude of services that could be provided to the TPPPS by the gambling enterprise in the contract. This requirement places the burden on the TPPPS to justify that they are not paying more than is appropriate for the level of services and facilities.

- A new paragraph (7) is added which will work in conjunction with the new paragraph (4) of subsection (c) of Section 12200.7 by requiring that documentation be provided that establishes the actual costs of advertising and equipment. Requiring the documentation be provided to the Bureau allows the reimbursement to be validated.
- A new paragraph (8) is added to expand upon a new subsection (j) of Section 12200.21. This provision requires that a full disclosure of any financial arrangements entered into within three years prior to the contract must be provided to the Bureau. While current regulations only require those arrangements that exist concurrent with the contract, this provision will allow the Bureau to ensure that no consideration was provided prior to the contract approval request that may have influenced the creation of the contract or attempts to circumvent the restrictions of statue or regulations relative to the contract. The period of three years is proposed as it is consistent with other statues requiring financial statements, such as sections 19880(b)(10), 19890(e)(1) and 19890.5(e)(1).
- A new paragraph (9) provides clarity that the Bureau is able to request additional information, as needed, so that the Bureau can be confident that the contract is not in violation of the provisions of regulation or law. This provision is necessary so that the regulations cannot be interpreted to limit the Bureau's investigatory authority.

A new subsection (c) is added to provide that a complete application for approval of the renewal of a contract would follow the same requirements as an initial application with the exception of the requirement to provide copies of the playing book forms. The different playing book form requirement reflects that the TPPPS is currently operating in the gambling establishment and copies can be provided that have already been completed. This allows the Bureau to see the practical use of the playing book form instead of just a blank copy. The process of contract renewal remains unchanged with the exception of those changes also being made on initial applications. Combining the two sections removes the need for repetitiveness.

Paragraph (4) of subsection (a) in the current regulation is renumbered as subsection (d), and details the method the Bureau must follow when either approving or disapproving the contract. This provision is modified to remove an unnecessary reference to amendments that is not appropriate in the initial/renewal approval process.

Current subsection (b) requires that an executed copy of the contract and any amendments along with any Bureau notices be maintained at the gambling establishment for review or copying by the Commission or Bureau. This provision is repealed as representatives of the Commission and Bureau already have access to these documents, and the gambling enterprise should not be required to maintain them for the Commission's or Bureau's use.

This change would not prevent local agencies from requiring that these documents be maintained on site, nor would it prevent the gambling enterprise from choosing to maintain the documents at their establishment.

Current subsection (c) requires that the contract term not exceed two years and that specific amendments may not be made without prior written approval of the Bureau. The portion of this subsection dealing within amendments is repealed. This is a non-substantive technical, editorial change as this part of the provision is duplicative of Section 12200.11. The part of this subsection limiting a contract to no more than a two-year term is retained and relocated to subsection (a) as subparagraph (E) of paragraph (1).

A new subsection (e) requires that a copy of the Bureau's notice of approval or disapproval be provided to the Commission. This moves the current requirement from subsection (b) of Section 12200.10C. Due to the renewal provisions being moved to this section, this change also includes the requirement that the Bureau provide the Commission a copy of any notice of approval or disapproval for renewal applications.

<u>Amend Section 12200.10A. Expedited Review and Approval of Proposition Player Contracts.</u>
This proposed action would renumber Section 12200.10A as Section 12200.10. This renumbered section continues the current expiated contract approval procedures and expands upon them.

Paragraph (2) of subsection (a) is revised to change the term "house" to "gambling enterprise." This change maintains consistency with other changes and clarifies that the contract is with the gambling enterprise and not the house. Section 19805 defines "house" as "…the gambling enterprise, and any owner, shareholder, partner, key employee, or landlord thereof." In the context of identifying the parties to the contract, the house is not the appropriate entity to fill that role. A key employee is just an employee of the business and while that person may be authorized to act in specific roles on behalf of the business, they are not a party to the contract or responsible for fulfilling the contract. Conversely, gambling enterprise, also defined in section 19805, means "…a natural person or an entity… that conducts a gambling operation…" As the party conducting the business, gambling enterprise is the more specific and relevant term to use to refer to a party to the contract.

A new paragraph (4) is added to subsection (a). The expedited review process requires that the new contract be substantially similar to the existing contract except that the TPPPS is different. In order to ensure that any newly approved contract is consistent with any changes to law or regulation, it might be necessary to prevent a contract from being approved under the expedited process. This paragraph provides this clarifying requirement, by preventing a contract from being approved if the Act or regulations are substantively revised.

A new paragraph (5) is added to subsection (a). Paragraph (1) of subsection (a) of Section 12200.9 provides a general requirement that all contracts must be approved by the Bureau

and specifies a number of other requirements, such as the contract cannot undermine the public trust, or cannot exceed a two-year term. The expedited review process is separate from the regular contract approval process, but there are still aspects that are relevant. This paragraph provides clarity that the separation of the processes is about the review and approval process and not the minimum standards a contract must meet.

Subsection (b) is revised to change the term "house" to "gambling enterprise." This change maintains consistency with other changes and clarifies that the contract is with the gambling enterprise and not the house. Section 19805 defines "house" as "…the gambling enterprise, and any owner, shareholder, partner, key employee, or landlord thereof." In the context of identifying the parties to the contract, the house is not the appropriate entity to fill that role. A key employee is just an employee of the business and while that person may be authorized to act in specific roles on behalf of the business, they are not a party to the contract or responsible for fulfilling the contract. Conversely, gambling enterprise, also defined in section 19805, means "…a natural person or an entity… that conducts a gambling operation…" As the party conducting the business, gambling enterprise is the more specific and relevant term to use to refer to a party to the contract.

Subsection (c) is revised to provide a non-substantive formatting correction. Additionally, paragraphs (1) through (5) of subsection (c) are deleted and replaced with a reference to the requirements of a complete application pursuant to paragraph (2) of subsection (a) of Section 12200.9. The previous list was an unnecessary duplication of that list, and therefore the removal of the duplicative language is non-substantive. Paragraph (6) of subsection (c) is the only provision that is different from the other list, and is retained and renumbered accordingly.

A new subsection (d) added. This provision is consistent with the new subsection (c) of Section 12200.9, and necessary for the same reasons.

<u>Amend Section 12200.10B. Review and Approval of Amendments to Proposition Player Contracts.</u>

This proposed action would renumber Section 12200.10B as Section 12200.11. This renumbered section continues the current amendment approval procedures and expands upon them.

Subsection (a) establishes the approval process for standard contract amendments. This provision is amended to clarify that any amendments, except for those provided for in subsection (b), must be approved by the Bureau before becoming effective. Additionally, non-sustentative grammatical, editorial changes in reference to the required form are made. Language is added to provide clarity that the amendment process cannot be utilized to circumvent the minimum standards provided for in paragraph (1) of subsection (a) of Section 12200.9. Finally, in conjunction with the repeal of Section 12200.10C, and with the changes in Sections 12200.9 and 12200.10, a requirement for Commission notification is added.

Subsection (b) provides an alternative approval process for a select list of contract terms. This approval process allows for the terms to be modified without Bureau approval and instead only requires notification within 10 days of the execution of the revised contract. This exception streamlines the approval process for these items, while still ensuring they are consistent with the contract protections of paragraph (1) of subsection (a) of Section 12200.9.

Current subsection (b) provides that paragraphs (3), (4) and (6) [renumbered as (3), (4) and (7)] of subsection (b) of Section 12200.7 are subject to this process. The adoption of a new paragraph (1) of subsection (b) of this section adds new paragraphs (5) and (6) and current paragraph (8) of subsection (b) of Section 12200.7 to this exception. Paragraphs (5), (6) and (8) of subsection (b) of Section 12200.7 deal with issues unrelated to the play of the game or any payment and so are items less likely to violate the provisions of paragraph (1) of subsection (a) of Section 12200.9. Notification to the Bureau allows for the monitoring of the contract while acknowledging that it is unlikely these issues present a danger to the public.

A new paragraph (2) is added to provide that payments made by the TPPPS to the gambling enterprise for advertising and equipment may be amended with only notification to the Bureau. These payments are restricted to no more than a proportionate share of the actual cost of the advertising or equipment, and the parties must provide documentation to show the actual cost. The Bureau will then be able to verify that payment does not exceed the appropriate amount. Streamlining the process for these reimbursements allows the parties to be able to effectively and efficiently operate their businesses without the additional burden of pre-approval. Verifying after the fact ensures compliance with the Act and regulations.

<u>Repeal Section 12200.10C. Submission of Contracts or Amendment to Commission.</u>
This section provides guidance to the Bureau on how it must communicate with the Commission during the contract approval process. The proposed action repeals this section.

Subsection (a) requires that the Bureau provide copies of contracts and amendments to the Commission for review and comment. This step in the process is extraneous and unnecessary. Currently this provision only requires that the Bureau provides the contract for comment but provides no requirement that any comments be considered, or that any approval or disapproval occur after the receipt of Commission comments. Section 19984 clearly provides authority to approve contracts to the Bureau while only providing regulatory authority to the Commission. As this provision only creates an extra step in the process, it is repealed. By repealing this provision, unneeded work is avoided for both Commission and Bureau staff, allowing the Bureau to more effectively and efficiently focus on approving and enforcing pertinent sections of the regulations and making the contract review process simpler and perhaps faster.

Subsection (b) is deleted and the provisions are incorporated into Sections 12200.9, 12200.10 and 12200.11. This provision requires that the Bureau provide copies of its notices of approval and disapproval to the Commission.

Repeal Section 12200.11. Extension of Proposition Player Contracts.
The proposed action repeals this section. This section provides a structure which, for the most part, is duplicative of Section 12200.9. As part of the changes in Section 12200.9, the non-duplicative provisions of this section are incorporated into the standard application approval process. The different provisions, such as the difference in playing book form submittal have been provided for. By combining the sections, the language of paragraph (1) of subsection (a) of Section 12200.9 is expanded to cover the renewal process. This expansion ensures that the protection provisions included in the regulations cannot be circumvented by renewing a contract.

Amend Section 12200.21. Compliance.
This section provides general guidelines and restrictions for the TPPPS contract process, including those provisions previously in the contract that are not contractual terms between the parties but regulatory restrictions placed on the parties. The proposed action also provides additional requirements or clarifications, many of which have been removed from other sections and amended into this section.

Subsection (a) provides a general requirement that TPPPS employees follow the game rules approved by the Bureau. Additionally, it allows a contract to contain provisions regarding the assignment of a permanent seat to the TPPPS, and exclusion of other TPPPS and gambling businesses. These last two provisions are deleted and moved to subsection (b) of Section 12200.7 as new paragraphs (5) and (6).

The current text of subsection (b) becomes paragraph (1), without change, and new paragraphs (2), (3) and (4) are added.

The new paragraph (2) of subsection (b) provides guidance that individuals with a “higher” level of licensure can also serve the functions of “lower” level licenses. This provision currently exists twice in the regulations, as subparagraph (C) of paragraph (12) of subsection (b) of Section 12200 and the first portion of subparagraph (C) of paragraph (23) of subsection (b) of Section 12200. These provisions provide clarification to both the licensed and registered individuals. These are functional provisions and not part of a definition and the inclusion twice is redundant. By moving the provisions to this section, unnecessary language is removed from the regulation and the clarification is put in a section more suitable to its function. This is a non-substantive technical, editorial change and has no effect.

The new paragraph (3) of subsection (b) provides a restriction to individuals who hold approvals to function both as a TPPPS employee and a gambling enterprise employee. This restriction prevents an individual from utilizing their third-party proposition player status within any gambling enterprise where they are employed. This restriction currently exists as paragraph (10) of subsection (b) of Section 12200.7. Currently this restriction is included in the contract and is therefore an issue enforced by the parties of the contract. This restriction addresses the possible perception that gambling may not be fairly administered, and should therefore be monitored and enforced by the Bureau. By moving this provision out of Section

12200.7 and into Section 12200.21, it becomes clear that the Bureau may investigate and enforce violations of this restriction. Since this provision has merely been relocated without change, the relocation has no regulatory effect.

The new paragraph (4) of subsection (b) limits the presence of the TPPPS at any specific table to no more than one owner, supervisor or proposition player. This restriction currently exists as paragraph (5) of subsection (b) of Section 12200.7. Currently this restriction is included in the contract and is therefore an issue enforced by the parties of the contract. This restriction addresses with the possible perception that gambling is not being fairly administered, and should therefore be monitored and enforced by the Bureau. By moving this provision out of Section 12200.7 and into Section 12200.21, it becomes clear that the Bureau may investigate and enforce violations of this restriction. Since this provision has merely been relocated without change, the relocation has no regulatory effect.

The new subsection (c) provides clarification that the TPPPS shall pay the same collection rate as any other participant in a controlled game. This restriction currently exists as paragraph (12) of subsection (b) of Section 12200.7; however, the language has been modified to provide clarity. The Bureau has the authority to approve collection rates[3] for a game, which provide for the fees collected by the gambling establishment. These rates are generally based upon the position (player or player-dealer) of an individual and may also depend on the amount being wagered by the individual. This provision provides clarity that, for the purposes of the payment of collection fees, the TPPPS is considered the same as any other player, which includes paying the same collection rate.

The new subsection (d) requires that any legal dispute between the parties needs to be reported to the Bureau. This provision currently exists as paragraph (16) of subsection (b) of Section 12200.7; however, the language has been modified. The requirement to report to the Commission has been eliminated in the revised language. Following implantation of the Governor's Reorganization Plan No. 2 of 2012 (GRP No. 2) the Bureau has been given the exclusive responsibility of investigating issues and reporting to the Commission. Therefore, it is not necessary or appropriate that legal disputes be reported to the Commission, as the Bureau should first investigate before reporting to the Commission.

The new subsection (e) provides that if any employee of the TPPPS is arrested in or removed from the gambling establishment or is involved in a dispute with a patron that results in the removal of one or more individuals, the parties must provide a report to the Bureau. This provision currently exists as paragraph (17) of subsection (b) of Section 12200.7; however, the language has been modified. The requirement to report to the Commission has been eliminated in the revised language. Post GRP No. 2 the Bureau has been given the exclusive responsibility or appropriate of investigating issues and reporting to the Commission. Therefore, it is not necessary that removals be reported to the Commission, as the Bureau should first investigate before reporting to the Commission.

[3] Section 19826, subdivision (g) and Penal Code section 337j, subdivision (f)

The new Subsection (f) provides that any incident of cheating reported by the TPPPS to the gambling enterprise must be reported to the Bureau within five days. This provision currently exists as paragraph (18) of subsection (b) of Section 12200.7; however, the language has been modified. The requirement to report to the Commission has been eliminated in the revised language. Post GRP No. 2 the Bureau has been assigned the exclusive responsibility of investigating issues and reporting to the Commission. Therefore, it is not necessary or appropriate that cheating be reported to the Commission, as the Bureau should first investigate before reporting to the Commission.

The new Subsection (g) provides guidelines for any tipping arrangement put in place as part of, or in addition to, the contracting process. Currently paragraph (20) of subsection (b) of Section 12200.7 provides that the tipping arrangement must be included as part of the contract. This provision caused confusion, as in some cases parties wanted to only allow for the TPPPS to tip at its discretion. As this wasn't an actual arrangement, the parties found it unclear what should be included and would only state that tipping is discretionary. This lack of specificity does not provide the Bureau with the information it requires to monitor the relationships between the two parties so more clarity is required. These restrictions deal with the perception that gambling is not being fairly administered, and should therefore be monitored and enforced by the Bureau. By moving this provision out of Section 12200.7 and into Section 12200.21, it becomes clear that the Bureau may investigate and enforce violations of this restriction.

Paragraph (1) of the new subsection (g) requires the TPPPS to provide its tipping policy as an addendum to the contract. The revisions to paragraph (20) of subsection (b) of Section 12200.7 remove the requirement that the tipping policy be included as part of the contract. Paragraph (1) of subsection (g) replaces that old requirement with a new one that allows for a tipping arrangement to be included in the contract, as is currently required, but also provides an additional requirement to cover situations where the parties have agreed to allow tipping but not to have a pre-arranged system. A TPPPS, as a business organization, would not allow its employees ultimate discretion to tip with company money, so this proposed new requirement would require whatever internal policy the TPPPS puts into place to direct its employees to be disclosed. It is critical that the Bureau have a complete understanding of the financial arrangements between the two parties, as is referenced many times throughout this proposed action, so that the Bureau can ensure that the relationship appropriately separates the financial interests of the gambling enterprise from the money wagered, won, or lost by the TPPPS.

Paragraph (2) of the new subsection (g) continues the restriction already present in paragraph (20) of subsection (b) of Section 12200.7, restricting any tipping arrangement or policy from including any percentage calculation.

Paragraph (3) of the new subsection (g) requires that the employee classifications of the gambling enterprise that are included in the tipping policy be provided. This information is required as further provisions limit the types of employees eligible to receive tips.

Paragraph (4) of the new subsection (g) prohibits any tipping arrangement or policy from providing tips to any employee of the gambling enterprise that is exercising any supervisory responsibility or any authority to make discretionary decisions that affect the result of the game during that particular shift. This restriction is critical, as it removes potential concerns that the TPPPS may be providing tips as a method of gaining advantage or influencing decisions. While it is common practice for any player in any particular game to tip as they desire, the TPPPS is, in most cases, the player with the most presence. Even if the TPPPS is tipping at a lower rate than any other individual player, when those players leave, the TPPPS is still present at the table. It is therefore a concern that the gambling enterprise employees may provide greater deference to the needs of the TPPPS as they come to understand that over the long run the TPPPS is providing a potentially significant portion of their tip income. By restricting tips from those with authority over the game, this potential incentive can be reduced and made clear that it is a reward for service and not any measure of earning interest in the game.

Paragraph (5) of the new subsection (g) provides clarity that a tip can be considered any monetary asset and not just a gambling chip or currency. This clarification is needed to minimize attempts to circumvent the provisions in this subsection and ensure the fairness of gambling in California.

The new subsection (h) provides that a TPPPS may not purchase, lease or control any gambling equipment related to a controlled game at a gambling establishment. This restriction currently exists as the second sentence of paragraph (21) of subsection (b) of Section 12200.7. This restriction deals with the perception that gambling is not being fairly administered, and should therefore be monitored and enforced by the Bureau. By moving this provision out of Section 12200.7 and into Section 12200.21, it becomes clear that the Bureau may investigate and enforce violations of this restriction.

The new subsection (i) provides that it is the responsibility of the gambling enterprise to ensure that the TPPPS follows all laws and regulations pertaining to controlled gambling. The addition of this provision is in conjunction with the repeal of paragraph (8) of subsection (b) of Section 12200.7. This repealed provision required that the parties agree in the contract that the services provided will be in compliance with all requirements of controlled gambling. This restriction deals with the perception that gambling is not being fairly administered, and should therefore be monitored and enforced by the Bureau. By moving this provision out of Section 12200.7 and into Section 12200.21, it becomes clear that the Bureau may investigate and enforce violations of this restriction. Additionally, the provision has been modified. Instead of requiring a mutual agreement between the parties that they will follow the law, this provision would place the requirement on the gambling enterprise. The gambling enterprise is the licensed entity offering the game, and has the responsibility of enforcing the rules in all cases, not just when related to proposition player services. This change makes the provision consistent with the status of the gambling enterprise in relation to the managing of the game, for which proposition player services are included.

The new subsection (j) provides that financial arrangements, relationship or transactions entered into during the contract period and between the TPPPS and gambling enterprise or any of their designated derivative parties or persons affiliated with them, must be disclosed to the Bureau with 10 days of their execution. This requirement deals with Bureau's ability to ensure that the gambling enterprise is sufficiently distanced from the funds wagered, won, or lost as part of a game, and should therefore be monitored and enforced by the Bureau. By moving this provision out of paragraph (15) of subsection (b) of Section 12200.7 and into Section 12200.21, it becomes clear that the Bureau may investigate and enforce violations of this restriction. The previous inclusion as part of the contract required that any new arrangement also requires an amendment to the contract. This is unnecessary as the scope of the notification has been broadened. Additionally, the change to notification is consistent with other changes included as part of this proposed action. This provision has also been modified in addition to its move. The requirement to disclose financial arrangements has been clarified to require other financial relationships and transactions. This helps to ensure that a full financial picture of the relationship between the two parties is clear to the Bureau. Finally, in conjunction with other changes to the regulation, the scope of this financial disclosure has been broadened to include the derivative parties and the affiliates of any specified persons. This broader scope of information will assist the Bureau in ensuring that there is no attempt to circumvent the intent of these provisions and the Act, namely the illicit transfer of money from those participating in the game (the TPPPS) and those offering the game (the gambling enterprise).

The new subsection (k) provides that neither the TPPPS nor the gambling enterprise may provide rebates. The addition of the TPPPS to the preclusion of providing rebates is necessary because of the relationship the TPPPS has as part of the game. While the TPPPS is a business that is licensed or registered with the Commission, during the play of the game it serves in the same role as any other individual participating in the game and not as an operator or in any other segregated role. Procedurally, it is strange to allow for one player in a game to provide rebates to another player while not giving that same option to every player.

The proposed changes in Chapter 10 are as follows:

<u>Amend Section 12560. Disciplinary Guidelines for Third-Party Providers of Proposition Player Services Licensees or Registrants.</u>
This section contains non-substantive revisions to correct and conform the references in paragraphs (7), (8), (9), (10), (11), and (19) of subsection (b) and paragraph (8) of subsection (d) to numerous changes made to the specified sections in Chapter 2.1. Additionally, to be consistent with subsection (k) of Section 12200.21, paragraph (19) of subsection (b) and paragraph (8) of subsection (d) of this section are revised to conform with the prohibition of rebates in all cases.

<u>UNDERLYING DATA</u>:

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

BUSINESS IMPACT:

The Commission has made an initial determination that the adoption of these regulations would have no significant statewide adverse economic impact directly affecting business, including the ability of California businesses to compete with businesses in other states.

This proposed action imposes some mandatory requirements on businesses. The regulation provides a clear process for determining the payment for services in a contract for proposition player services and sets a clear process for receiving approval from the Bureau. Costs associated with pursuing a contract would be voluntarily assumed by the gambling enterprise as a contract with a TPPPS is only required if the gambling enterprise desires such services. The TPPPS, however, is required to have a TPPPS contract in order to operate, so any additional costs are not voluntarily assumed. Parties currently engaged in a contract will find an increase in the documentation and justification required under this revised process, though the specifics will depend on the complexity of their contract.

SPECIFIC TECHNOLOGIES OR EQUIPMENT:

These regulations do not mandate the use of specific technologies or equipment.

ECONOMIC IMPACT ASSESSMENT/ANALYSIS:

This proposal is only intended to clarify the contract amounts currently being determined and should not cause a significant impact on the contract prices. Additional parts of the proposal include clarification of current contract approval processes and the shift of operative or compliance provisions to other regulation sections for enforcement by the Bureau. No significant additional burden has been placed upon either the gambling enterprise or the TPPPS, or either's employees.

CREATION OR ELIMINATION OF JOBS WITHIN THE STATE OF CALIFORNIA:

These regulations are designed to assist the Bureau in its duty of ensuring that a contract for third-party services does not cause the gambling enterprise to have an interest in the funds wagered, lost, or won. These regulations modify and clarify existing requirements, and should not alter current practices significantly enough to alter a gambling enterprise's decision to contract, or not contract, for third-party services. Therefore, it has been determined that the proposed action will not have an impact on the creation or elimination of jobs.

CREATION OF NEW BUSINESSES OR ELIMINATION OF EXISTING BUSINESSES WITHIN THE STATE OF CALIFORNIA:

These regulations are designed to assist the Bureau in its duty of ensuring that a contract for third-party services does not cause the gambling enterprise to have an interest in the funds wagered, lost, or won. These regulations modify and clarify existing requirements, and should not alter current practices significantly enough to alter a gambling enterprise's decision to contract, or not contract, for third-party services. Because the number of cardrooms in California

is capped there can be no new cardrooms created. This proposal will not eliminate any cardrooms, as the contract amounts cannot be of a value significant enough that the cardrooms cannot operate without it. Likewise, this proposal will not eliminate any existing TPPPS as there should be no significant change in the contract amounts. This proposal will neither discourage nor encourage the creation of new TPPPS companies as it will not significantly alter market conditions. Therefore, it has been determined that the proposed action will not have an impact on the creation of new businesses or the elimination of existing businesses.

EXPANSION OF BUSINESSES CURRENTLY DOING BUSINESSES WITHIN THE STATE OF CALIFORNIA:

These regulations are designed to assist the Bureau in its duty of ensuring that a contract for third-party services does not cause the gambling enterprise to have an interest in the funds wagered, lost, or won. These regulations modify and clarify existing requirements, and should not alter current practices significantly enough to alter a gambling enterprise's decision to contract, or not contract, for third-party services. Therefore, it has been determined that the proposed action will not have an impact on the expansion of businesses currently doing business in California.

BENEFITS OF THE REGULATIONS:

This proposed action will have the benefit of clarifying the TPPPS contract approval process by identifying how any payment by the TPPPS to the gambling enterprise shall be determined. Additionally, the proposed action will provide the Bureau with clearer criteria to use in reviewing and approving contracts, and ensures that the information required for review is clear and available. The gambling enterprise and TPPPS will benefit by having a clear understanding of what payments are allowed to ensure that their businesses are properly segregated and to help prevent illegal banking situations from occurring.

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, would be as effective and less burdensome to affected private persons than the proposed regulation, or more cost-effective to affected private person and equally effective in implementing the statutory policy or other provision of law.
Set forth below are the alternatives that were considered and the reasons each alternative was rejected:

(1) Maintain Status Quo: Current regulations are effective and operative and therefore the current contract review process could continue without any change by the Commission. Current regulations do not, however, provide the level of clarity desired by the Bureau to effectively ensure that the contracts do not include "payments for services or facilities that are substantially disproportionate to the value of services or facilities provide" as the current regulations require in paragraph (1) of subsection (c) of section 12200.7. The contract is only required to identify the total charges in the three categories of services,

facilities and advertising but does not require the inclusion of specific costs in the detailed list.

(2) No Longer Allow Payment to the Gambling Enterprise by the TPPPS: The second alternative considered and rejected by the Commission was to disallow any payment by the TPPPS to the gambling enterprise. Current regulations allow for a payment for services, facilities and advertising to be provided by the TPPPS to the gambling enterprise as long as those payments are not based on the funds wagered, lost or won with some other additional restrictions to ensure the separation of the two parties. This option was considered, not because the current practice is in violation of any specific provision, but because it could create a perception of impropriety and could lead to possible collusion. This alternative was not accepted as the gambling enterprise is required to incur expenses due to the existence of another business operating on its premises and it is reasonable to require that other business to pay those costs. Additionally, the use of facilities and services on the premises should not be borne by the host business but by the user just as any other business would rent space and pay for services received. The restrictions provided for in the proposed regulations provide the Bureau the tools required to ensure that the costs are not inappropriate in relation to the level of services provided, and that the payments do not provide the gambling enterprise interest in the funds wagered, lost or won.

(3) No Longer Allow the Tipping of Gambling Enterprise Employee's by the TPPPS: The third alternative considered and rejected by the Commission was to disallow the tipping of gambling enterprise employees by the TPPPS. Current regulations allow for tipping if a tipping provision is included in the Bureau-approved contract. This option was considered, not because the current practice is in violation of any specific provision, but because it could create a perception of impropriety and could lead to possible collusion. Additionally, it could be considered an additional avenue through which funds are transferred by the TPPPS to the gambling enterprise by providing a subsidization of the gambling enterprise's labor costs. This alterative was not accepted as during the actual play of the game the TPPPS serves in a role equivalent to any other player and there is nothing to prevent any other player from providing a gratuity. The requirement that any payment agreement be included in the contract provides for monitoring by the Bureau to ensure that no inappropriate level of payment is being provided.