

TITLE 4.
CALIFORNIA GAMBLING CONTROL COMMISSION
NOTICE OF PROPOSED REGULATORY ACTION
AND PUBLIC COMMENT PERIOD CONCERNING
ACCOUNTING AND FINANCIAL REPORTING REQUIREMENTS FOR GAMBLING
ENTERPRISES, THIRD-PARTY PROVIDERS OF PROPOSITION PLAYER
SERVICES, AND GAMBLING BUSINESSES
CGCC-GCA-2014-04-R

NOTICE IS HEREBY GIVEN that the California Gambling Control Commission (Commission) is proposing to take the action described below in the Informative Digest and Policy Statement Overview. Any interested person, or his or her authorized representative, may present statements or arguments orally or in writing relevant to the proposed regulatory action at a public hearing to be held at **10:00 a.m. on July 23, 2014**, at 2399 Gateway Oaks Drive, Suite 100, Sacramento, CA 95833.

WRITTEN COMMENT PERIOD

Written comments relevant to the proposed regulatory action, including those sent by mail, facsimile, or e-mail, may be submitted to the Commission at any time during the public comment period. To be eligible for the Commission's consideration, all written comments must be **received at its office no later than 5:00 p.m. on June 16, 2014**. Written comments should be directed to one of the individuals designated in this notice as a contact person. **Comments sent to persons and/or addresses other than those specified under Contact Persons, or received after the date and time specified above, will be included in the record of this proposed regulatory action, but will not be summarized or responded to regardless of the manner of transmission.**

ADOPTION OF PROPOSED ACTION

After the close of the public comment period, the Commission, upon its own motion or at the instance of any interested party, may thereafter formally adopt the proposals substantially as described below or may modify such proposals if such modifications are sufficiently related to the original text. With the exception of technical or grammatical changes, the full text of any modified proposal will be available for 15 days prior to its adoption from the person designated in this Notice as contact person and will be mailed to those persons who submit oral or written testimony related to this proposal or who have requested notification of any changes to the proposal.

AUTHORITY AND REFERENCE

Pursuant to the authority vested by sections 19811, 19823, 19824, 19840, 19841, 19853, 19857 and 19984 of the Business and Professions Code; and to implement, interpret or make specific sections 19805, 19823, 19824, 19826, 19841 and 19984 of the Business and Professions Code, the Commission is proposing to adopt the following changes to Chapter 1 and to add Chapter 5 of Division 18 of Title 4 of the California Code of Regulations:

INFORMATIVE DIGEST AND POLICY STATEMENT OVERVIEW

INTRODUCTION:

The Commission is the state agency charged with the administration and implementation of the California Gambling Control Act (Act).¹ The Commission is authorized to adopt regulations governing accounting and financial reporting requirements for gambling enterprises.² The Commission is also authorized to adopt regulations governing licensing requirements, disclosures, approvals, and financial audit requirements for third-party providers of proposition player services (TPPPS),³ as well as to approve or disapprove transactions, events, and processes as provided in the Act.⁴

While accounting and financial reporting requirements were previously established, the current requirements apply only to gambling enterprises. The need to also apply these requirements to TPPPS companies and gambling businesses has become apparent. TPPPS companies and gambling businesses are a large part of the gambling industry, and yet lack the oversight placed upon the gambling enterprises. Adding these regulations in Chapter 5 will provide uniform standards for accounting and financial reporting for gambling enterprises, TPPPS companies and gambling businesses.

Consolidation of repetitive or generally accepted terms and provisions into Chapter 1 of the Commission's regulations will provide simple, clear and uniform terms and procedures.

EFFECT OF REGULATORY ACTION:

In general, this proposed action has been drafted in an attempt to adopt accounting and financial reporting requirements for TPPPS companies and gambling businesses that are equivalent to the existing accounting and financial reporting requirements for gambling enterprises. This proposed action also attempts to consolidate and simplify repetitive definitions and provisions into Chapter 1, which applies to all of the Commission's regulations.

ANTICIPATED BENEFITS OF PROPOSED REGULATION:

It is anticipated that the proposed regulations will have the benefit of providing uniform accounting and financial reporting and record maintenance for all gambling entities. The procedures will assure the public that those with a TPPPS or gambling business license conduct

¹ Business and Professions Code, Division 8, Chapter 4, section 19800 et seq.

² Business and Professions Code section 19841.

³ Business and Professions Code section 19984.

⁴ Business and Professions Code section 19824.

their financial activities appropriately and with proper oversight. This will provide transparency, clarity and uniformity for gambling enterprises, TPPPS companies and gambling businesses. These proposed regulations will also provide simple and uniform terms and provisions that would apply throughout the Commission's regulations.

EXISTING LAW:

Business and Professions Code section 19827, subdivision (a), paragraph (1), subparagraphs (A), (D) and (E), provide the Department of Justice (Department)⁵ the investigative authority to access, inspect, and audit documents from any licensed premises in order to determine compliance with the Act.

Business and Professions Code section 19840 provides the Commission the authority to adopt regulations and requires that those regulations take into consideration the operational differences of large and small establishments.

Business and Professions Code section 19841, subdivision (a), paragraph (2), provides that the regulations of the Commission shall prescribe the information to be furnished by any licensee or registrant concerning business activities, organizational structure, and financial affairs.

Business and Professions Code section 19841, subdivision (d), provides the Commission the authority to adopt regulations that require owner licensees to report and keep records of transactions involving cash or credit. This section also provides that the Commission's regulations may include requirements for owner licensees to file with the Department reports similar to those required to be filed pursuant to Title 31 of the United States Code and Title 31 of the Code of Federal Regulations.

Business and Professions Code section 19841, subdivision (h), provides the Commission the authority to adopt regulations that prescribe minimum procedures for owner licensees to exercise effective control over their internal fiscal and gambling affairs. This shall include but not be limited to the safeguarding of assets and revenues; prescribing the manner in which compensation from games and gross revenues shall be computed and reported; and the provision of reliable records, accounts, and reports, including reports to be submitted to the Department.

Business and Professions Code section 19841, subdivision (i), provides the Commission the authority to adopt regulations for the adoption and use by owner licensees of internal audits, whether performed by qualified internal auditors or by certified public accountants, to test and evaluate proper compliance with the minimum standards required in subsection (h).

Business and Professions Code section 19841, subdivision (j), provides the Commission the authority to adopt regulations that require periodic financial reports from each owner licensee.

⁵ In the Act, "department" refers to the Department of Justice. While the Act assigns certain powers and authority to the department, in actual practice the responsibility for fulfilling the obligations imposed upon the department is delegated to the Bureau of Gambling Control, pursuant to Business and Professions Code section 19810.

Business and Professions Code section 19841, subdivision (l), provides the Commission the authority to adopt regulations that formulate a uniform code of accounts and accounting classifications to ensure consistency, comparability, and effective disclosure of financial information.

Business and Professions Code section 19841, subdivision (m), provides the Commission the authority to adopt regulations that prescribe the intervals at which information in subdivision (j) shall be furnished to the Department.

Business and Professions Code section 19841, subdivision (n), provides the Commission the authority to adopt regulations that require audits to be conducted of the financial statements of all owner licensees whose gross annual income equals or exceeds a specified amount, in accordance with generally accepted auditing standards. This subdivision also allows for compilations and reviews to be made of a licensee's records by a California-licensed independent certified public accountant.

Business and Professions Code section 19841, subdivision (o), provides the Commission the authority to adopt regulations that restrict, limit, or otherwise regulate any activity related to the conduct of controlled gambling that is consistent with the purposes of the Act.

Business and Professions Code section 19984, subdivision (b), provides the Commission the authority to establish reasonable criteria for any person or entity that provides proposition player services to gambling establishments. Under this section, the Commission may impose disclosures, approvals, conditions, or limitations as it deems necessary to protect the integrity of controlled gambling.

Business and Professions Code section 19984, subdivision (c), provides the Department the authority to perform background checks, financial audits, and other investigatory services as needed, pursuant to Commission regulations, to assist the Commission in regulating third-party providers of proposition player services.

SPECIFIC PROPOSAL:

This proposed action would make the following specific changes in Chapter 1 and Chapter 7, and adds Chapter 5 to Division 18 of Title 4 of the California Code of Regulations:

CHAPTER 1. GENERAL PROVISIONS.

Amend Section 12002. General Definitions.

With the addition of a new Chapter 5, certain definitions limited to Chapter 2.1 and 2.2 will now also apply in Chapter 5. Additionally, some terms are used throughout the regulations. For simplicity and clarity, these terms would be added in the general definitions section.

Duplications of these terms would then be removed accordingly. The following amendments are proposed:

- Subsection (b) – Quotations are added around the term “Bureau” as a non-substantive conforming editorial change for consistency.

- Subsection (g) – The term “dealer’s bank” would be moved from paragraph (2) of subsection (b) of Section 12400 and added in Section 12002. The phrase “gambling establishment” would be changed to “gambling enterprise.”
- Subsection (h) – The term “drop” would be moved from paragraph (3) of subsection (b) of Section 12400 and added in Section 12002, and references to TPPPS players would be added. The phrase “gambling establishment” would be changed to “gambling enterprise.” Finally, the current definition of the term “drop” may unintentionally include tournament fees; therefore the definition is amended to exclude tournament fees.
- Subsection (i) – A comma is added after “19816” in the first sentence and the word “the” is deleted after “vacant,” in the second sentence. These are non-substantive grammatical changes.
- Subsection (j) – The term “fiscal year” would be moved from paragraph (4) of subsection (b) of Section 12400 and added in Section 12002.
- Subsection (k) – The term “gambling business” would be added.
- Subsection (m) – The term “jackpot” would be moved from paragraph (8) of subsection (b) of Section 12400 and added in Section 12002. The phrase “authorized game” would be changed to “controlled game” as defined in section 19805. Finally, the term “predetermined” would be changed to “specified.”
- Subsection (n) – The term “licensee” would be added.
- Subsection (o) – The term “player’s bank” would be moved from paragraph (11) of subsection (b) of Section 12400 and would be amended to include the monies a TPPPS company has on deposit to be consistent with the Bureau of Gambling Control (Bureau) regulations. The phrase “gambling establishment” would be changed to “gambling enterprise.”
- Subsection (r) – The term “third-party providers of proposition player services” or “TPPPS” would be added.
- The remaining subsections would be renumbered accordingly.

Add Section 12003. General Requirements.

Several requirements, such as requiring records to be maintained in English, are included in multiple sections throughout the Commission’s regulations. Moreover, requirements such as allowing electronic communication and storage have been repetitively added to individual chapters of the regulations as they are not yet generally allowed. These repetitive provisions would be included in a general requirements section for simplicity, consistency, and clarity. Duplications of these requirements could then be removed accordingly.

- Subsection (a) – The requirement that all books, accounts, financial records, and documents required by the Commission or the Bureau shall be in English would be added.
- Subsection (b) – The requirement that all records required by the Commission or the Bureau shall be maintained for five years, unless otherwise specified, would be added. The requirement that these records shall be stored in a secure location on the premises of the gambling establishment, main offices of the TPPPS company or gambling business,

or other location approved by the Bureau would also be added. The requirement that any change in an approved location be reported to the Bureau within five business days of the change and that the location would be deemed approved if not disapproved by the Bureau, would be added.

- Subsection (c) – The current requirement of Section 12405 that each licensee must provide the Bureau with copies of any records upon request would be added to Section 12003. To comply with subsection (d), if hardcopies of documents stored in another form are required by the Bureau, the licensee would need to be able to comply with that request.
- Subsection (d) – The option to store and submit records in either a permanent form or other media, unless otherwise specified, would be added.

Add CHAPTER 5. ACCOUNTING AND TRANSACTION APPROVALS.

Adding “Chapter 5” would permit the organization and consolidation of the accounting and financial reporting regulations to clearly establish that the sections contained in Chapter 5 will apply to gambling enterprises, TPPPS companies, and gambling businesses.

Add Article 1. Accounting and Financial Reporting.

Add Section 12311 – Definitions.

The current Section 12400 would be renumbered as Section 12311, with some amendments for accuracy and clarity. The following amendments are proposed:

- Subsection (a) – The current subsection (a) of Section 12400 would be retained in Section 12311 and amended to reference the definitions in Section 12002.
- Subsection (b), paragraph (1) – The current definition for “Group I Licensee” in paragraph (5) of subsection (b) of Section 12400 would be retained.
- Subsection (b), paragraph (2) – The current definition for “Group II Licensee” in paragraph (6) of subsection (b) of Section 12400 would be retained.
- Subsection (b), paragraph (3) – The current definition for “Group III licensee” in paragraph (7), subsection (b) of Section 12400 would be retained and amended to refer to licensees with a reported gross income of \$500,000 or more but less than \$2 million for the preceding fiscal year.
- Subsection (b), paragraph (4) – The term “Group IV licensee” would be added to refer to licensees with a reported gross income of less than \$500,000 for the preceding fiscal year.
- Subsection (b), paragraph (5) – The current definition for “jackpot administrative fee” in paragraph (9) of subsection (b) of Section 12400 would be retained.
- Subsection (b), paragraph (6) – The current definition for “licensee” in paragraph (10) of subsection (b) of Section 12400 would be retained and amended to include those possessing a TPPPS or gambling business license or registration, for the purposes of this chapter.
- Section 12400 – The definition for the term “authorized game” would be deleted from paragraph (1) of subsection (b) of Section 12400. Paragraphs (2), (3), (4), and (8) of subsection (b) of Section 12400 would be moved to Section 12002 as discussed above.

Add Section 12312 – Record Retention and Maintenance; General Provisions.

Section 12312 consolidates several current requirements for accounting and financial reporting into one section, adding references to TPPPS companies and gambling businesses where appropriate.

- Subsection (a) – The current requirement in Section 12405 to maintain financial records for seven years within California would become subsection (a) of Section 12312, with the added qualification that the retention requirement applies to the records required by this article.
- Subsection (b) – The current requirement of subsection (a) of Section 12401 to maintain accurate, complete, and legible records in sufficient detail to support the amount of revenue reported to the Bureau in renewal applications would become subsection (b) of Section 12312. Additionally, the phrase “gross revenue as defined in Business and Professions Code section 19805(r)” would be replaced with “all transactions pertaining to financial activities.”
- Subsection (c) – The current requirement of subsection (b) of Section 12401 to maintain various accounting records would become subsection (c) of Section 12312. References to TPPPS companies and gambling businesses would be added.
- Subsection (d) – The current requirements of subsection (a) of Section 12402 to maintain a uniform chart of accounts and accounting classifications in order to prepare a complete set of financial statements would become subsection (d) of Section 12312, with minor changes. The words “and” instead of “or” and the clarification of “particular” would be incorporated. The requirement that the statement of operations is to be a detailed statement of operations would be added. Also, alternative but acceptable terminology for the records needed would be included. The requirement that the chart of accounts be included with the initial application of a TPPPS company or gambling business for review and approval by the Bureau would be added. Requirements for submissions of the chart of accounts in Section 12402, subsections (b) and (c), would be removed as no longer necessary.
- Subsection (e) – The current requirements of subsection (d) of Section 12402 to keep a general ledger and to use a double-entry accounting system would become subsection (e) of Section 12312.

Add Section 12313 – Financial Statements and Reporting Requirements.

The current Section 12403 would be renumbered as Section 12313 with non-substantive edits for clarity and simplicity. Additionally, the following amendments are proposed:

- Subsection (a) – The current reporting requirements of Section 12403 would be amended to include TPPPS companies and gambling businesses.
- Subsection (a), paragraph (4) – The reference to those in Group III with gross revenue of less than \$500,000 per year would be changed to refer to the new Group IV.
- Subsection (b) – The repetitive provision in paragraphs (2), (3), and (4) of subsection (b) of Section 12403 would be merged into subsection (b) of Section 12313 for simplicity, consistency and clarity. The remaining subsections would be renumbered accordingly.

- Subsection (c) – The phrase “and the Commission” would be added to allow the Commission to also receive a copy of the annual financial statements to be used to make determinations on an applicant’s suitability for licensure and other approvals.

Add Section 12315 – Records and Reports of Monetary Instrument Transactions for Gambling Enterprises.

The current Section 12404 would be renumbered as Section 12315, with the following amendments:

- The phrase “for Gambling Enterprises” would be added to the title of Section 12315 as the requirements of this section are specific to gambling enterprise activities.
- Subsection (b) – This subsection would be amended to refer to Chapter X of Title 31 of the Code of Federal Regulations.

Add Section 12316 – Unclaimed or Abandoned Property.

The current Section 12410 is renumbered as Section 12316, with the following changes.

- The references to “licensee” would be changed to “gambling enterprise.”

CHAPTER 7. CONDITIONS OF OPERATION FOR GAMBLING ESTABLISHMENTS.

Repeal Article 4. Accounting and Financial Reporting.

Article 4, including Sections 12400 through 12410, would be repealed and its provisions moved to Chapter 1 or to the new Chapter 5 as described above.

CONSISTENCY OR COMPATIBILITY WITH EXISTING STATE REGULATIONS

The Commission has evaluated this regulatory action and determined that the proposed regulations are neither inconsistent nor incompatible with any other existing state regulations.

The Commission is vested with jurisdiction and supervision over gambling establishments and over all persons or things having to do with the operations of gambling establishments in California.⁶ The scope and content of the Commission’s regulations is generally set forth in section 19841. Section 19841 provides the authority for the Commission to adopt regulations governing accounting and financial reporting requirements for gambling enterprises. Section 19824 provides the Commission with the authority to approve or disapprove transactions, events, and processes as provided in the Act. The Commission is also authorized to adopt regulations governing licensing requirements, disclosures, approvals, and financial audit requirements for TPPPS companies under section 19984, subdivision (b).

While the Bureau has also been granted some authority to adopt regulations (section 19826), that authority is limited to the adoption of regulations reasonably related to its specified duties and responsibilities. These proposed regulations are not inconsistent or incompatible with any

⁶ Business and Professions Code section 19811.

Bureau regulation (Title 11, CCR, Division 3), nor do they fall within the Bureau's authority to adopt regulations.

COMPARABLE FEDERAL LAW

There are no existing federal regulations or statutes comparable to the proposed regulations.

FISCAL IMPACT ESTIMATES

FISCAL IMPACT ON PUBLIC AGENCIES INCLUDING COSTS OR SAVINGS TO STATE AGENCIES OR COSTS/SAVINGS IN FEDERAL FUNDING TO THE STATE: None.

NON-DISCRETIONARY COST OR SAVINGS IMPOSED UPON LOCAL AGENCIES: None.

MANDATE IMPOSED ON ANY LOCAL AGENCY OR SCHOOL DISTRICT FOR WHICH PART 7 (COMMENCING WITH SECTION 17500) OF DIVISION 4 OF THE GOVERNMENT CODE REQUIRES REIMBURSEMENT: None.

COST TO ANY LOCAL AGENCY OR SCHOOL DISTRICT FOR WHICH PART 7 (COMMENCING WITH SECTION 17500) OF DIVISION 4 OF THE GOVERNMENT CODE REQUIRES REIMBURSEMENT: None.

EFFECT ON HOUSING COSTS: None.

IMPACT ON BUSINESS:

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.

The following studies/relevant data were relied upon in making the above determination:

This regulatory proposal does not add any accounting or financial reporting requirement for gambling enterprises. The changes would only require TPPPS companies and gambling businesses to meet the same standards as gambling enterprises, as appropriate. Therefore, it was determined that there would be no cost or other adverse impact on gambling enterprises associated with the proposed action.

This regulatory proposal sets forth requirements for record maintenance and submittal of financial information that each TPPPS company and gambling business should already have in place. These records would be used to submit tax information to the Internal Revenue Service and the Franchise Tax Board. The requirement for the submission of an audit, review, compilation, or federal tax filings is adjusted by gross income to ensure that the financial reporting is required to be submitted in a way that is appropriate and affordable for each licensee. Therefore, it was determined that there would be no significant adverse economic impact directly affecting TPPPS companies or gambling businesses.

The proposed regulations will consolidate repetitive general provisions into one chapter making them applicable, when appropriate, throughout the Commission's regulations. Additionally, a general provision to allow for the use of electronic communication and storage of records will provide an option that licensees may choose as a faster, easier and more cost-effective method of compliance where appropriate.

COST IMPACT ON REPRESENTATIVE PRIVATE PERSON OR BUSINESS:

The Commission is not aware of any cost impacts that a representative private person or business would necessarily incur in reasonable compliance with the proposed action.

EFFECT ON SMALL BUSINESS:

The Commission has determined that the proposed regulatory action would not have a significant effect on small businesses, if any affected TPPPS company or gambling business would qualify as a small business. The entities that might qualify as a small business would be allowed to submit a copy of the business's federal tax return and maintain the documentation necessary to support the tax return, which is already required by the Internal Revenue Service. The only additional requirement imposed by these regulations is that these businesses would need to submit a copy to the Bureau and the Commission.

RESULTS OF ECONOMIC IMPACT ASSESSMENT/ANALYSIS

IMPACT ON JOBS/NEW BUSINESSES:

The Commission has determined that this regulatory proposal will not have a significant impact on the creation of new jobs or businesses, the elimination of jobs or existing businesses, or the expansion of businesses in California.

The basis for this determination is that this proposed action imposes accounting and financial record maintenance requirements that should already be in place in the normal course of business. This proposed action only formalizes these processes and requires annual submissions of financial records.

BENEFITS OF PROPOSED REGULATION:

The amendments would better implement various aspects of the Act and provide further clarification as to the procedures required to maintain and submit accounting and financial records, by applying the requirements, as appropriate, to TPPPS companies and gambling businesses as well as gambling enterprises. This will provide transparency, clarity and uniformity concerning the financial activities of gambling enterprises, TPPPS companies and gambling businesses.

These proposed regulations will provide uniform accounting and financial reporting and record maintenance for all gambling entities. These procedures will assure the public that those with a TPPPS or gambling business license conduct their financial activities appropriately and with proper oversight. The proposed regulations would also consolidate and simplify repetitive terms

and general provisions by placing these provisions in Chapter 1, to be applicable to all sections of the Commission's regulations.

Any interested person may present statements or arguments orally or in writing relevant to the above determinations at the above-mentioned hearing.

CONSIDERATION OF ALTERNATIVES

The Commission must determine that no reasonable alternative considered by the Commission or that has otherwise been identified and brought to the attention of the Commission would be 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 action, or would be more cost-effective to affected private persons and equally effective in implementing the statutory policy or other provision of law.

INITIAL STATEMENT OF REASONS, INFORMATION AND TEXT OF PROPOSAL

The Commission has prepared an Initial Statement of Reasons and the exact language for the proposed action and has available all the information upon which the proposal is based. Copies of the language and of the Initial Statement of Reasons, and all of the information upon which the proposal is based, may be obtained at the hearing or prior to the hearing upon request from the Commission at 2399 Gateway Oaks Drive, Suite 220, Sacramento, CA 95833-4231.

AVAILABILITY AND LOCATION OF THE RULEMAKING FILE AND THE FINAL STATEMENT OF REASONS

All the information upon which the proposed action is based is contained in the Rulemaking File that will be available for public inspection and copying at the Commission's office throughout the rulemaking process. Arrangements for inspection and/or copying may be made by contacting the backup contact person named below.

Upon its completion, the Final Statement of Reasons will also be available. A copy of the Final Statement of Reasons may be obtained, once it has been prepared, by making a written request to one of the contact persons named below or by accessing the Commission's Web site listed below.

CONTACT PERSONS

All comments and inquiries concerning the substance of the proposed action should be directed to the following **primary** contact person:

James B. Allen, Manager
Regulatory Actions Unit
California Gambling Control Commission

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2399 Gateway Oaks Drive, Suite 220, Sacramento, CA 95833-4231
Telephone: (916) 263-4024
Fax: (916) 263-0499
E-mail: Jallen@cgcc.ca.gov

Requests for a copy of the Initial Statement of Reasons, proposed text of the regulation, modified text of the regulation, if any, or other technical information upon which the proposed action is based should be directed to the following **backup** contact person:

Helen Geoffroy, Regulatory Actions Analyst
Regulatory Actions Unit
California Gambling Control Commission
2399 Gateway Oaks Drive, Suite 220, Sacramento, CA 95833-4231
Telephone: (916) 263-4904
Fax: (916) 263-0499
E-mail: hgeoffroy@cgcc.ca.gov

WEB SITE ACCESS

Materials regarding this proposed action are also available on the Commission's Web site at www.cgcc.ca.gov.