

CALIFORNIA GAMBLING CONTROL COMMISSION
FINAL STATEMENT OF REASONS
CGCC-GCA-2014-04-R

HEARING DATE:

October 22, 2014

SUBJECT MATTER OF PROPOSED REGULATIONS:

Accounting and Financial Reporting Requirements for Gambling Enterprises, Third-party Providers of Proposition Player Services, and Gambling Businesses

SECTIONS AFFECTED:

California Code of Regulations, Title 4, Division 18: Sections 12002, 12003, 12311, 12312, 12313, 12315, 12316, 12400, 12401, 12402, 12403, 12404, 12405, 12406, and 12410

UPDATED INFORMATION:

The Initial Statement of Reasons, as published on May 2, 2014, is included in the file and is hereby incorporated by reference as if fully set forth herein. The information contained therein is updated as follows:

PROPOSED ACTION:

This proposed action will make changes in Division 18, Title 4 of the California Code of Regulations. The proposed changes are as follows:

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, it is necessary for these terms to be added to the general definitions to provide understanding for these terms regardless of where they are used in the Commission's regulations. Duplications of these terms are removed accordingly. The following amendments are made:

- 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” is moved from paragraph (2) of subsection (b) of Section 12400 and added in Section 12002 to allow this term to be uniformly used throughout the regulations of the California Gambling Control Commission (Commission). The phrase “the total amount of” is changed to “any and all” for clarity and simplicity. This change is necessary because the use of the word “total” can be

interpreted narrowly to exclude some monies; “any and all” is a more accurate and inclusive phrase. The phrase “gambling establishment” is changed to “gambling enterprise” for accuracy and clarity. Business and Professions Code section 19805 defines “gambling enterprise” as a person or entity that conducts a gambling operation, and “gambling establishment” as the physical room or rooms where controlled gambling occurs. This change is necessary because this term refers to the conduct of controlled gambling and not the physical space, so “gambling enterprise” is the more appropriate term.

- Subsection (h) – The term “drop” is moved from paragraph (3) of subsection (b) of Section 12400 and added in Section 12002 to allow this term to be uniformly used throughout the Commission’s regulations. References to TPPPS and gambling business players are added as they also pay player collection fees to play in controlled games. The phrase “the total amount of” is changed to “any and all” for clarity and simplicity. This change is necessary because the use of the word “total” can be interpreted narrowly to exclude a portion of the fees collected from patrons; “any and all” is a more accurate and inclusive phrase. The word “compensation” is changed to “player collection fees” for specificity and is necessary to avoid confusion with other types of payments such as jackpot fees. The phrase “gambling establishment” is changed to “gambling enterprise” for accuracy and clarity. Business and Professions Code section 19805 defines “gambling enterprise” as a person or entity that conducts a gambling operation, and “gambling establishment” as the physical room or rooms where controlled gambling occurs. This change is necessary because this term refers to the conduct of controlled gambling and not the physical space, so “gambling enterprise” is the more appropriate term. Finally, the current definition of the term “drop” may unintentionally include other fees; therefore the definition is amended to exclude tournament fees, jackpot collections, and payments under contracts for third-party proposition player services, for consistency and clarity in the use of this term.
- Subsection (i) – Subsection (g) is renumbered as 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” is moved from paragraph (4) of subsection (b) of Section 12400 and added in Section 12002 to allow this term to be uniformly used throughout the Commission’s regulations.
- Subsection (k) – The term “gambling business” is added to reference persons registered or licensed in accordance with Chapter 2.2, and to allow this term to be uniformly used throughout the Commission’s regulations.
- Subsection (h) is renumbered as subsection (l).
- Subsection (m) – The term “jackpot” is moved from paragraph (8) of subsection (b) of Section 12400 and added in Section 12002 and the phrase “appended to the play of an authorized game in a gambling establishment” is deleted. The phrase “in which the” is replaced with “where the,” the word “predetermined” is changed to “specified,” and the phrase “occurring in the play of a controlled game” is added. The term “predetermined” is changed to “specified” for accuracy and is necessary to better reflect how a jackpot is

achieved according to the individual game rules. The word “authorized game” is replaced with “controlled game” for simplicity and consistency with the Act and the Commission’s regulations. This rewording more accurately reflects current usage of the term, and moving this term to Section 12002 is necessary to allow this term to be uniformly used throughout the Commission’s regulations.

- Subsection (n) – The term “licensee” is added to allow this term to be uniformly used throughout the Commission’s regulations.
- Subsection (o) – The term “player’s bank” is moved from paragraph (11) of subsection (b) of Section 12400 to allow this term to be uniformly used throughout the Commission’s regulations. The definition is amended to include the monies a TPPPS company has on deposit to be consistent with this term’s interpretation and usage by the Bureau of Gambling Control (Bureau). The phrase “the total amount of” is changed to “any and all” for clarity and simplicity. This change is necessary because the use of the word “total” can be interpreted narrowly to exclude a portion of the monies a player has on deposit; “any and all” is a more accurate and inclusive phrase. The phrase “gambling establishment” is changed to “gambling enterprise” for accuracy and clarity. Business and Professions Code section 19805 defines “gambling enterprise” as a person or entity that conducts a gambling operation, and “gambling establishment” as the physical room or rooms where controlled gambling occurs. This change is necessary because this term refers to controlled gambling and not the physical space, so “gambling enterprise” is the more appropriate phrase.
- Subsection (i) is renumbered as subsection (p).
- Subsection (j) is renumbered as subsection (q).
- Subsection (r) – The term “third-party providers of proposition player services” or “TPPPS” is added to reference persons registered or licensed in accordance with Chapter 2.1, and to allow this term to be uniformly used throughout the Commission’s regulations.

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, provisions such as allowing electronic communication and storage of records have been repetitively added to individual chapters of the regulations as they are not yet generally allowed. These repetitive provisions are included in a general requirements section for simplicity and clarity. Duplications of these provisions are 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 is added. This provision is necessary to provide clarity and common understanding between the licensee and the Commission and Bureau as well as to uniformly apply this provision throughout the Commission’s regulations.
- Subsection (b) – The requirement that all records required by the Commission or the Bureau shall be maintained for five years, unless otherwise specified, is added. Multiple

sections in the current regulations mandate a five-year retention period for various records required by the Act and by regulation. Moreover, the Act and regulations require record retention when those records are subject to an audit or review by the Bureau. Five years is a generally applied retention period for other businesses and industries when the documentation is retained for potential audits or reviews. This provision is necessary to adopt a reasonable and uniform baseline for record retention which will create simplicity and clarity throughout the Commission's regulations. However, this baseline can be adjusted in individual regulation sections for circumstances where less or greater retention periods would be appropriate.

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 is also added. These provisions simplify the record maintenance requirements throughout the regulations, but allow for variances when necessary. This provision is necessary to ensure that the records are safely maintained in a location known by the Bureau for audit and compliance purposes.

The requirement that any change in an approved location reported to the Bureau is deemed approved if not disapproved by the Bureau within 30 days of receipt of the written notice is added. This provision is necessary to allow the licensee to proceed with the location change and to clarify when the change would be deemed approved.

- Subsection (c) – The current requirement of Section 12405 that each licensee must provide the Bureau with copies of any records upon request is added to Section 12003 to be applicable to all records required to be maintained by the Commission or the Bureau. To comply with subsection (d), if hardcopies of documents stored in another form are required by the Bureau, the licensee must be able to comply with that request. These provisions are necessary to maintain efficient and consistent procedures for the Bureau to obtain records for investigatory and auditing purposes.
- Subsection (d) – The option to store and submit records in either a permanent form or other media unless otherwise specified is added. As electronic methods of storage and communication become more common for licensees and the Bureau, this option is necessary to allow the licensee to use the methods of communication and required document storage that best serve the licensee's business needs.

Add CHAPTER 5. ACCOUNTING AND TRANSACTION APPROVALS.

Adding Chapter 5 permits the reorganization and consolidation of the accounting and financial reporting regulations to clearly establish that the sections contained in Chapter 5 apply to gambling enterprises, TPPPS companies, and gambling businesses.

Add Article 1. Accounting and Financial Reporting.

Add Section 12311 – Definitions.

The current Section 12400 is renumbered as Section 12311, with some amendments for accuracy and clarity. The meaning of the words and terms in this article may not be consistent with the meaning of similar words or terms used in other existing regulations. As a result, these

definitions are necessary to ensure that the proposed regulations are clear, concise and easy to understand. The following amendments are made:

- Subsection (a) – The current subsection (a) of Section 12400 is 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 is retained.
- Subsection (b), paragraph (2) – The current definition for “Group II Licensee” in paragraph (6) of subsection (b) of Section 12400 is retained.
- Subsection (b), paragraph (3) – The current definition for “Group III licensee” in paragraph (7) of subsection (b) of Section 12400 is 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. In the current Section 12403, the reporting requirements for Groups I and II are provided in paragraphs (1) and (2) of subsection (a). In paragraphs (3) and (4), different reporting requirements are provided for different income levels within Group III. Special reporting options are provided for those in Group III with gross revenue of less than \$500,000 annually. This accommodation is compliant with section 19840, which provides that the regulations of the Commission shall take into consideration the operational differences of large and small establishments. However, the use of the same term, Group III, to reference two distinct revenue levels is unnecessary and unclear. Because this subgroup of Group III (gross revenue of less than \$500,000) is appropriately granted this accommodation for financial reporting, for clarity and simplicity, it is necessary that this subgroup is identified separately as Group IV. Therefore, the definition for the term “Group III” is amended to refer to licensees with a reported gross income of \$500,000 or more but less than \$2 million, and the term “Group IV” is added to refer to those making less than \$500,000 annually.
- Subsection (b), paragraph (4) – The term “Group IV licensee” is added to refer to licensees with a reported gross income of less than \$500,000 for the preceding fiscal year. In the current Section 12403, the reporting requirements for Groups I and II are provided in paragraphs (1) and (2) of subsection (a). In paragraphs (3) and (4), different provisions are provided for different income levels within Group III. Special reporting options are provided for those in Group III with gross revenue of less than \$500,000 annually. This accommodation is compliant with section 19840, which provides that the regulations of the Commission shall take into consideration the operational differences of large and small establishments. However, the use of the same term, Group III, to reference two distinct revenue levels is unnecessary and unclear. Because this subgroup of Group III (gross revenue of less than \$500,000) is appropriately granted this accommodation for financial reporting, for clarity and simplicity, it is necessary that this subgroup is identified separately as Group IV. Therefore, the term “Group IV” is added to refer to those making less than \$500,000 annually.
- Subsection (b), paragraph (5) – The current definition for “jackpot administrative fee” in paragraph (9) of subsection (b) of Section 12400 is retained.
- Subsection (b), paragraph (6) – The current definition for “licensee” in paragraph (10) of subsection (b) of Section 12400 is retained and amended to include, for the purposes of

this chapter, those possessing a TPPPS or gambling business license or registration in addition to the section 19805 definition of “owner licensee.” This change is necessary to incorporate TPPPS companies and gambling businesses into the existing accounting and financial reporting provisions, and to add simplicity and clarity.

- Section 12400 – The definition for the term “authorized game” in paragraph (1) in subsection (b) of Section 12400 is not included in Section 12311, and is deleted. Use of the term “controlled game,” as defined in section 19805, is more consistent and clear, as this term is used throughout the Act, related sections of the Penal Code, and the regulations of the Commission and the Bureau. The term “authorized game” is only used in the Section 12400 definition for “jackpot,” which has now been amended to use the term “controlled game.” Therefore the term “authorized game” is deleted because it is inconsistent and unnecessary. Paragraphs (2), (3), (4), and (8) of subsection (b) of Section 12400 are 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 has 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 has become subsection (b) of Section 12312. Additionally, the phrase “gross revenue as defined in Business and Professions Code section 19805(r)” is replaced with “all financial activities.” This change is necessary because “gross revenue,” as defined in section 19805, refers only to a cardroom’s gross income, and therefore would not apply to TPPPS companies or gambling businesses. The current provision is also incompatible with the provisions of Section 12313, which requires that the preparation of financial statements incorporate all financial activities. Therefore, the phrase “all transactions pertaining to financial activities” is more accurate, consistent, and inclusive.
- Subsection (c) – The current requirement of subsection (b) of Section 12401 to maintain various accounting records has become subsection (c) of Section 12312. The phrase “as applicable” is added as some records are specific to gambling enterprises and some are specific to TPPPS companies and gambling businesses. It is necessary to add references to TPPPS companies and gambling businesses to apply the requirements for maintenance of relevant records to TPPPS companies and gambling businesses as well as gambling enterprises.
- Subsection (c), paragraph (4) – The phrase “separated by gaming activity” is added. This change is necessary to conform with the Bureau’s audit procedures.

- 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 have become subsection (d) of Section 12312, with minor changes. The words “and” instead of “or” and the clarification of “particular” are incorporated for clarity of the requirement. The requirement that the statement of operations is to be a detailed statement of operations is added to more clearly explain the reporting requirement. Also, alternative but acceptable terminology for the records required is necessary to add clarity and understanding. 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 is added. This provision is necessary to allow the Bureau to confirm that the licensee has an acceptable chart of accounts for use during an audit. Requirements for submissions of the chart of accounts in Section 12402, subsections (b) and (c), are removed as these submissions are no longer necessary. If the chart of accounts is needed at any time after the initial application, the Bureau may request the document in accordance with Section 12003.
- Subsection (e) – The current requirements of subsection (d) of Section 12402 to keep a general ledger and to use a double-entry accounting system have become subsection (e) of Section 12312, with no change other than the correction of the referenced subsection in this section and a hyphen placed between “double” and “entry” for correct spelling.

Add Section 12313 – Financial Statements and Reporting Requirements.

The current Section 12403 is renumbered as Section 12313 with non-substantive edits for clarity and simplicity, as described below. Additionally, the following amendments are made:

- Subsection (a) – The word “A” is replaced with “Each” and the phrase “as applicable” is added to clarify that each licensee shall prepare financial statements for their entity as appropriate. This is a non-substantive change for clarity and simplicity. The reference to “gambling operation” is changed to “gambling enterprise” for accuracy. Business and Professions Code section 19805 defines “gambling enterprise” as a person or entity that conducts a gambling operation, and “gambling operation” means exposing for play one or more controlled games. This change is necessary because this phrase refers to the entity’s financial activities as a whole and not the action of conducting controlled gaming, so “gambling enterprise” is the more appropriate term. The reference to a “licensee” owning or operating lodging, etc., is changed to refer to “gambling enterprise” for accuracy and clarity. TPPPS companies and gambling businesses do not operate lodging, food, beverage, or other non-gambling operations connected with their controlled gaming activities. This particular provision references gambling enterprises only, so this change is necessary to clearly reflect this specification now that TPPPS companies and gambling businesses are added.
- Subsection (a), paragraph (3) – The phrase “with a gross revenue of \$500,000 or more per year” is deleted, as this information is included in the definition for Group III in Section 12311.
- Subsection (a), paragraph (4) – The reference to those in Group III with gross revenue less than \$500,000 per year is changed to refer to the new Group IV. While only three income groups are identified in the current regulations, the reporting option in this

paragraph is for a subgroup of Group III, consisting of those making less than \$500,000 within the Group III definition of those making less than \$2 million. This subgroup is accommodated separately in the term “Group IV,” as proposed in Section 12311. Therefore, this reporting option is amended to reflect the new term “Group IV.”

- Subsection (b) – The repetitive provision in paragraphs (2), (3), and (4) of subsection (b) of Section 12403 is merged into subsection (b) of Section 12313 for simplicity and clarity. The remaining subsections are renumbered accordingly.
- Subsection (c) – The phrase “and the Commission” is 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.

The Commission inadvertently deleted the requirement for licensees to submit annual financial statements to the Commission in its Section 100 regulation changes implementing the Governor’s Reorganization Plan of 2012 (GRP No. 2). The Section 100 change rationale for the deletion indicated that “The references to the Commission also receiving financial statements [and] documents are deleted as unnecessarily duplicative. The Bureau has the responsibility for investigations under the GRP No. 2 amendment of section 19826(a). It is not necessary that licensees be required to send the same documents to both the Bureau and the Commission.”

While the Bureau uses the annual financial statements for investigative purposes, the Commission also needs to receive the annual financial statements. They are used by the Commission to obtain current data on gambling enterprise revenues and other financial information. The Commission needs timely access to the information provided within the annual financial statements, including gambling enterprise revenues, to respond to requests from Commissioners and the Administration. This information is not always readily available to the Commission from other sources.

- Subsection (e) – The phrase “by the Bureau or the Commission” is added as a non-substantive change that is necessary to clarify by whom the fraud or illegal acts are suspected.

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

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

- The phrase “for Gambling Enterprises” is added to the title of Section 12315 as the requirements of this section are specific to gambling enterprise activities.
- Subsection (b) – This subsection is merged with subsection (c) for clarity and simplicity.
- Subsection (c) – This subsection moves and consolidates the provisions of subsections (b) and (c) of Section 12404 into subsection (b) of Section 12315. This change is necessary to better reflect record maintenance requirements for documentation required by federal law.

This subsection is amended to refer to Chapter X of Title 31 of the Code of Federal Regulations. On March 1, 2011, the Financial Crimes and Enforcement Network

(FinCEN) transferred its regulations from 31 CFR Part 103 to 31 CFR Chapter X as part of an ongoing effort to increase the efficiency and effectiveness of its regulatory oversight. 31 CFR Chapter X is organized by generally applicable regulations and by industry-specific regulations. The provisions that are applicable to casinos and card clubs (cardrooms), including all of the sections currently listed in Section 12404, are now found in 31 CFR Chapter X, Part 1021 (revised as of July 1, 2011). There have been no substantive changes made to the underlying regulations as a result of this transfer and reorganization.

While subsection (b) requires compliance with federal law, it is the records maintenance provisions for this documentation that are addressed in this subsection. The details of the information already required by federal law are deleted as unnecessary.

- Subsection (d) is renumbered (c), accordingly.

Add Section 12316 – Unclaimed or Abandoned Property.

The current Section 12410 is renumbered as Section 12316.

- For clarity and consistency, the provisions in this subsection are numbered.
- The references to “licensee” are changed to “gambling enterprise” because the requirements of this section are specific to gambling enterprise activities.

CHAPTER 7. CONDITIONS OF OPERATION FOR GAMBLING ESTABLISHMENTS.

Repeal Article 4. Accounting and Financial Reporting.

Article 4, including Sections 12400 through 12410, is repealed and its provisions moved to Chapter 1 or to the new Chapter 5 as described above. Article 4 is currently in Chapter 7, which contains regulations for the conditions of operation of gambling establishments. Because the accounting and financial reporting regulations now apply to TPPPS companies and gambling businesses as well as gambling enterprises, including these regulations in a chapter designated for gambling establishment operations is no longer appropriate. Moving the regulations to a chapter that will apply the requirements uniformly to gambling establishments, TPPPS companies and gambling businesses is necessary to add clarity, consistency and understanding.

UNDERLYING DATA:

In addition to the information discussed in the Initial Statement of Reasons, the Commission also considered the following information: None.

REQUIRED DETERMINATIONS:

LOCAL MANDATE:

A mandate is not imposed on local agencies or school districts.

BUSINESS IMPACT:

The Commission has made a determination that the proposed regulatory action 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 determination is based on the following facts or evidence/documents/testimony:

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 is 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 are 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 preparation and submission of financial records is appropriate and affordable for each licensee. No comments were received from any TPPPS or gambling business representative during the public comment periods that claim a significant adverse economic impact to their businesses as a result of these regulations. Therefore, it was determined that there is no significant adverse economic impact directly affecting TPPPS companies or gambling businesses.

The proposed regulations 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 provides an option that licensees may choose as a faster, easier and more cost-effective method of compliance where appropriate.

FINDING RE. APPLICABILITY OF REPORTING REQUIREMENTS TO BUSINESSES:¹

The Commission finds that if the requirement for gambling enterprises, TPPPS companies and gambling businesses to submit copies of annual financial statements to the Bureau and Commission is determined to be a reporting requirement, that requirement is necessary for the health, safety and welfare of the people of this state. This finding is based on the following:

Gambling is the quintessential cash business and having financial information regarding those businesses engaged in gambling operations and controlled gaming is a vitally important part of properly regulated gambling. Public trust that gambling will not endanger public health, safety, or welfare requires comprehensive measures to ensure that gambling is conducted honestly and competitively. Public trust and confidence can only be maintained by strict regulation of all persons, practices, associations, and activities related to gambling operations and controlled gaming. In order to effectuate state policy as declared in the Act, the Commission may impose requirements for disclosures, approvals, conditions, or limitations as it deems necessary to protect the integrity of controlled gaming in this state. In general, the proposed action was

¹ Government Code sections 11346.3 (d).

drafted to establish uniform procedures and standards to assist the Commission and the Bureau in meeting their oversight responsibilities under the Act.²

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.

This determination is based on the fact that this regulatory proposal will not impose any significant cost or other adverse economic impact on licensees, as discussed above under “Business Impact.” Furthermore, this regulatory proposal would have no effect on any other business or job.

BENEFITS OF PROPOSED REGULATION:

These 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 their financial activities appropriately and with proper oversight. This will provide transparency, clarity and uniformity concerning the financial activities of 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. Among these, the proposed regulations will allow electronic communication and storage of records to be accepted, when appropriate, throughout the regulations. This will provide an option for faster, easier, and more cost-effective methods of meeting regulatory requirements.

CONSIDERATION OF ALTERNATIVES:

No reasonable alternative to the regulations that was considered by, 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, is as effective and less burdensome to affected private persons than the proposed action, or is more cost-effective to affected private persons 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) Eliminate the Accommodation for Licensees With Less Than \$500,000 in Reported Gross Income: Paragraph (4) of Subsection (a) of Section 12313 includes a provision that permits a licensee with a gross income for the year of less than \$500,000, and is

² Specifically, Business and Professions Code sections 19801 (g), (h), (k) and (n), 19823, 19826, and 19984 (b).

unable to produce financial statements, to submit their federal tax forms for that year. The alternative considered and rejected by the Commission was to eliminate the current accommodation. This alternative would require all licenses to submit financial statements annually.

This alternative was rejected because it would negatively impact the lowest income licensees. This alternative is also inconsistent with current practice. The federal income tax form accommodation was adopted by the Commission in 2003, in accordance with section 19840 of the Business and Professions Code, to take into consideration the operational differences of large and small gambling enterprises.

COMMENTS, OBJECTIONS OR RECOMMENDATIONS / RESPONSES:

The following public comments/objections/recommendations were made regarding the proposed action³ during the public comment periods:

I. 45-DAY WRITTEN COMMENT PERIOD

The following written comments/objections/recommendations were received regarding the text of the proposed action during the 45-day written comment period that commenced May 2, 2014 and ended June 16, 2014:

A. 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 are added in the general definitions for Division 18. Duplications of these terms have been removed accordingly.

1. Subsection (g) – The term “dealer’s bank” is moved from paragraph (2) of subsection (b) of Section 12400 and added in Section 12002. The phrase “gambling establishment” is changed to “gambling enterprise.”

- a. **Alan Titus, Artichoke Joe’s, in a letter dated June 16, 2014 (Mr. Titus):** The use of the word “total” is not clear and creates confusion. Instead, Mr. Titus suggests amending the text as follows:

“(g) ‘Dealer’s bank’ means any and all monies a dealer has on deposit with the gambling enterprise or is assigned from the cage bank or chip trays.”

Response: This comment was accepted, and the proposed action was modified, as suggested, to accommodate it.

2. Subsection (h) – The term “drop” is moved from paragraph (3) of subsection (b) of Section 12400 and added in Section 12002, and references to TPPPS players are

³ The descriptions of the proposed changes are based on the regulation text originally published May 2, 2014.

added. The phrase “gambling establishment” is changed to “gambling enterprise.” Finally, the current definition of the term “drop” may unintentionally include tournament fees; therefore the definition is amended to expressly exclude tournament fees.

- a. **David Fried, California Grand Casino and Oaks Card Club, in a letter dated June 16, 2014 (Mr. Fried); and Mr. Titus:** Mr. Fried comments that the definition should exclude services and facilities payments from TPPPS companies. Mr. Fried also comments that this definition for “drop” includes jackpot collections, and questions if this is intentional. Mr. Titus comments that the use of the word “total” is not clear and creates confusion. As the definition is written, a portion of the compensation collected from patrons would not be considered to be “drop.”

Mr. Fried suggests amending the text as follows:

“(h) ‘Drop’ means the total amount of compensation collected from patrons or TPPPS companies by a gambling enterprise to play in controlled games, not including tournament fees or payments under approved contracts for Third-Party Proposition Player Services.”

Mr. Titus suggests amending the text as follows:

“(h) ‘Drop’ means any and all compensation collected from patrons or TPPPS companies by a gambling enterprise to play in controlled games, not including tournament fees.”

Response: These comments were accepted, and the proposed action was modified as follows to accommodate them:

“(h) ‘Drop’ means any and all player collection fees received from patrons or TPPPS companies by a gambling enterprise to play in controlled games, not including tournament fees, or payments under contracts for Third-Party Proposition Player Services.”

3. Subsection (m) – The term “jackpot” is moved from paragraph (8) of subsection (b) of Section 12400 and added in Section 12002. The phrase “authorized game” is changed to “controlled game” as defined in section 19805. Finally, the term “predetermined” is changed to “specified.”
- a. **Mr. Fried:** This definition confuses promotions and jackpots. A jackpot is a type of promotion where the prize is based on the outcome of the hand or achieving a designated hand. Participation prizes are also a type of promotion, but are not jackpots. The current definition would include both jackpot awards and participation prizes. Instead, the definition should refer to the specific type of

promotions that are prizes awarded based on a specified result occurring in the play of the game. Mr. Fried suggests amending the text as follows:

“(m) ‘Jackpot’ means a gaming activity where the prize is determined by specified criteria determined in the play of a controlled game.”

Response: This comment was accepted, and the proposed action was modified as follows to accommodate it:

“(m) ‘Jackpot’ means a gaming activity where the prize is awarded based on specified criteria occurring in the play of a controlled game.”

4. Subsection (o) – The term “player’s bank” is moved from paragraph (11) of subsection (b) of Section 12400 and is amended to include the monies a TPPPS company has on deposit. The phrase “gambling establishment” is changed to “gambling enterprise.”

- a. **Mr. Titus:** The use of the word “total” is not clear and creates confusion. The status of a portion of the monies a player has on deposit is left unclear. Instead, Mr. Titus suggests amending the text as follows:

“(o) ‘Players bank’ means any and all monies a patron or a TPPPS company has on deposit with the gambling enterprise.”

Response: This comment was accepted, and the proposed action was modified, as suggested, to accommodate it.

B. 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.

1. The current requirement of subsection (b) of Section 12401 to maintain various accounting records becomes subsection (c) of Section 12312. References to TPPPS companies and gambling businesses are added.

- a. **Nathan DaValle, Assistant Bureau Chief, Bureau of Gambling Control, in a letter dated June 16, 2014 (Mr. DaValle):** The Bureau would like to ensure that detailed records are maintained to track that the monies paid out are approved, not excessive, and are maintained for each specific jackpot. Mr. DaValle suggests changing the proposed text of paragraph (4) of subsection (c) to read as follows:

“(4) Records, separated by gaming activity, of all monies contributed by the gambling enterprise, jackpot monies collected from

patrons, and monies withdrawn for either jackpot administrative fees or payment to patrons.”

Response: This comment was accepted, and the proposed action was modified, as follows, to accommodate it.

“(4) Records, separated by gaming activity, of all jackpot monies contributed by the gambling enterprise, jackpot monies collected from patrons, and monies withdrawn for either jackpot administrative fees or payment to patrons.”

C. Section 12313. Financial Statements and Reporting Requirements.

The current Section 12403 is renumbered as Section 12313 with non-substantive edits for clarity and simplicity.

1. Subsection (a), paragraph (4) – The reference to those in Group III with gross revenue of less than \$500,000 per year is changed to refer to a new Group IV.
 - a. **Mr. DaValle:** The Bureau is concerned about the option to submit a federal tax return in lieu of the financial statements. Since an income tax return is derived from the financial statements, the licensee should be able to provide the statements. Mr. DaValle suggests that clauses 1 and 2 of subparagraph (A) be deleted and the requirement to engage an independent accountant to perform a compilation of the licensee’s annual financial statements in clause 1 be added to subparagraph (A), as follows:

“A Group IV licensee shall prepare financial statements that include, at a minimum, a statement of financial position and a statement of income or a statement of operations. If the licensee is unable to produce the financial statements, it shall engage an independent accountant licensed by the California Board of Accountancy to perform a compilation of the licensee’s annual financial statements in accordance with standards for accounting and review services or with currently applicable professional accounting standards. Management may elect not to provide footnote disclosures as would otherwise be required by generally accepted accounting principles.”

Response: This comment was considered, but was rejected. The current regulatory provision of Section 12403 that allows for the submission of a federal tax return is only applicable if the licensee is unable to produce financial statements. Subsection (a) states “A licensee shall prepare financial statements covering all financial activities...” Subsection (a), paragraph (4), subparagraph (A), also states “A Group IV licensee shall prepare financial statements...” The submission of federal tax forms for Group IV licensees only applies “if the licensee is unable to produce financial statements...” This is a current provision relating to what is now a subset of Group III (i.e., licensees with a gross revenue

of less than \$500,000 per year), but has become Group IV under the proposed action. In other words, under the current regulation, a Group III licensee with gross revenue of less than \$500,000 per year that is unable to produce financial statements is permitted to submit a copy of a federal income tax return, as specified. Other than the creation of a new Group IV, there is no difference between the current regulation and the proposed action. Group IV licensees are those with gross revenue of less than \$500,000 per year.

According to the Final Statement of Reasons for the current regulation (CGCC-GCA-2003-02-R), this provision was included as a less expensive method of submitting financial information for those licensees with the lowest revenues. Business and Professions Code section 19840 provides that the Commission shall take into consideration the operational differences of large and small establishments to the extent appropriate. To delete the current provision permitting the submission of federal tax forms in limited circumstances would remove this less expensive and burdensome method and impose an adverse economic impact on those licensees who may be the least likely to have the resources necessary to hire an accountant.

In a review of this matter, no requirement could be found for the use of financial statements in the preparation of federal or state tax returns. In some instances, licensees' tax returns may be clearer and more concise than the supporting documentation used to prepare them. Furthermore, that supporting documentation would be available to the Bureau for audit just as it would be to the IRS.

2. Subsection (c) – The phrase “and the Commission” is 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.
 - a. **M. Robbins, in a letter received June 3, 2014:** The reinsertion of “and the Commission” is not in accordance with the Governor’s Reorganization Plan No. 2 (GRP No. 2). The submission of the financial statements to both the Bureau and the Commission is unnecessarily duplicative. In accordance with GRP No. 2, section 19826 provides that the Bureau investigates and is “to receive and process,” so the Commission should get this information from the Bureau. Requiring the licensees to submit a copy to both the Commission and the Bureau would require staff at both the Commission and Bureau to copy financial statements instead of one person at the Bureau, and therefore be a burden upon the taxpayers as well as contrary to the intentions of GRP No. 2. Robbins suggests that the text be amended to remove “and the Commission” and suggests that the Commission request financial statements from the Bureau.

Response: This comment was considered, but was rejected. Licensees have submitted copies of financial statements to both the Commission and the Bureau since 2003. This requirement is not inconsistent with GRP No. 2 or Business and

Professions Code section 19826. The general purpose of GRP No. 2 was to eliminate inefficiencies and separate the policy functions of the Commission from the licensing, investigation, compliance, and enforcement functions of the Bureau. Business and Professions Code section 19826, as amended by GRP No. 2, requires the Bureau to “receive and process *applications* for any license, permit, or other approval, and to collect related fees.” (Emphasis added.) That section also requires the Bureau to investigate the qualifications of applicants, as specified.

As indicated in the Commission’s Initial Statement of Reasons, while the Bureau uses the annual financial statements for investigative purposes, the Commission also uses these financial statements on a regular, ongoing basis for non-investigative purposes (to make determinations on an applicant’s suitability for licensure and other approvals). Upon further review, it has been determined that it would be more efficient overall for licensees to resume providing the financial statements to the Commission when they provide these statements to the Bureau, as this would ensure that the Commission has timely access to the most current financial statements used in making Commission decisions.

The suggested alternative is more burdensome to the Commission, Bureau and licensees, as it would require the Commission to submit a request to the Bureau for financial statements and require the Commission to await a response from the Bureau. As a result, this could cause delays in making suitability determinations for licensure and other approvals which, in turn, could negatively impact applicants and licensees.

There were no further comments, objections, or recommendations received regarding the proposed action within the initial 45-day written comment period.

II. JULY 23, 2014 REGULATION HEARING

The following comments/objections/recommendations were received regarding the text of the proposed action during the regulations hearing held July 23, 2014:

A. Section 12002. General Definitions.

With the addition of a new Chapter 5, certain definitions previously limited to Chapters 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 are added in the general definitions for Division 18. Duplications of these terms are removed accordingly.

1. Subsection (h) – The term “drop” is moved from paragraph (3) of subsection (b) of Section 12400 and added in Section 12002, and references to TPPPS players are added. The phrase “gambling establishment” is changed to “gambling enterprise.” Finally, the current definition of the term “drop” may unintentionally include tournament fees; therefore the definition is amended to expressly exclude tournament fees.

- a. **Misty Trejo, Bureau of Gambling Control:** Based on the summary of 45-day written comments document, it looks like the definition of “drop” will be changed to refer to “any player collection fees received” instead of “compensation.” For jackpots, we call the player contribution a “jackpot collection fee.” In the MICS [minimum internal control standards] regulations those [jackpot collection fees] have to be segregated from regular player collection fees.⁴ In proposed Section 12312 (c)(4) licensees have to track all of their jackpot money. I don't think that they [jackpot collection fees] are going to be confused with the player collection fees because they're segregated, and they have to account for their jackpot money separately from their regular collection fees or, in this case, the drop. I am comfortable with this definition with the changes recommended in the 45-day written comments document.

Response: This comment was considered and accepted, but no additional modification was necessary.

- b. **Mr. Fried:** The jackpot fee is a mandatory fee for those clubs that take a separate jackpot fee; so some people might interpret player collection fees to include jackpot fees. If you want a clean definition that just refers to the revenue of the club, then the word “jackpots” should be added to the phrase that begins, “not including tournament fees, ...”

Response: This comment was accepted, and the proposed action was modified as follows to accommodate it:

“(h) ‘Drop’ means any and all player collection fees received from patrons or TPPPS companies by a gambling enterprise to play in controlled games, not including tournament fees, jackpot collections, or payments under contracts for proposition player services.”

2. Subsection (m) – The term “jackpot” is moved from paragraph (8) of subsection (b) of Section 12400 and added in Section 12002. The phrase “authorized game” is changed to “controlled game” as defined in section 19805. Finally, the term “predetermined” is changed to “specified.”
- a. **Mr. Fried:** A jackpot is a really large prize you get when you have a great hand beat by another great hand. The problem that I was concerned about in my previous comment [See comment I.A.2.a.] is defining it so broadly that if you're just participating in the game and you get a discount on food that's a gaming activity because the criteria or the eligibility is you're participating in the game. So my comment was exclude what I call “participation awards” and focus on a prize that you get because something happens in the play of the hand or the play of the game. That may mean that things like bonus bets are swept in by this definition. A bonus is a bonus prize; a jackpot is a jackpot prize, and they're both determined by things that happen in the play of the game. If you want to use the

⁴ Title 4, California Code of Regulations, Section 12384 (a)(2).

word “jackpot” in a really narrow way, then the definition may need to be changed, but I think what's in the recommended response is better than the prior draft which swept in participation awards.

Response: This comment was considered, but was rejected. This comment appears to incorrectly use “bonus bet” and “bonus” as synonymous terms when they refer to two distinctly different things. A bonus bet is included and approved by the Bureau in game rules; a bonus is a gaming activity and is approved as such. In fact, bonus and jackpot are essentially synonymous terms since they are both gaming activities, prizes awarded based on specified criteria occurring in the play of a controlled game, are funded by players, and are paid by the gambling enterprise from the fund created by the player contributions. Therefore, it would not be inappropriate if bonuses are “swept in by this definition.” On the other hand, a bonus bet is not a gaming activity and does not operate like a gaming activity, and would not be “swept in by this definition.”

3. Subsection (r) – The term “third-party providers of proposition player services” or “TPPPS” is added to allow this term to be uniformly used throughout the Commission’s regulations.

- a. **Mr. Fried:** This definition refers to a business entity, and I think it should refer to a person. You can have a sole proprietor that's a third-party provider or a gambling business. So I think it should be “business entity or person,” or it should just say “person.”

Response: This comment was accepted, and the proposed action was modified as follows to accommodate it:

“(r) ‘Third-party providers of proposition player services’ or ‘TPPPS’ or ‘TPPPS company’ means a person that is licensed or registered in accordance with Chapter 2.1 of this division.”

This comment is also applicable to the definition of “gambling business” in subsection (k). Therefore, subsection (k) was also modified as follows to accommodate it:

“(k) ‘Gambling business’ means a person that is registered or licensed in accordance with Chapter 2.2 of this division. ‘Gambling business’ does not include the provision of proposition player services.”

The term “person” is used in both subsections (k) and (r) because that term, as defined in the Act,⁵ includes not only individuals, but also all types of business entities, including sole proprietorships.

⁵ Business and Professions Code section 19805, subdivision (ae), defines “person” to include “a natural person, corporation, partnership, limited partnership, trust, joint venture, association, or any other business organization.”

B. Section 12313. Financial Statements and Reporting Requirements.

The current Section 12403 is renumbered as Section 12313 with non-substantive edits for clarity and simplicity.

1. Subsection (a), paragraph (4) – The reference to those in Group III with gross revenue of less than \$500,000 per year is changed to refer to a new Group IV.
 - a. **Frances Asuncion, Bureau of Gambling Control:** The Bureau submitted a comment⁶ on page 6, line 19, requesting that the words “in lieu of” be removed. It's important for our audit staff to collect financial statements so that they can review and possibly audit certain line items. We would like that to be considered because it's important to not only have a tax return but also to have their financial statements. And this particular group, group four, should be required to have financial statements.

Response: This comment was considered, but was rejected. The current regulatory provision of Section 12403 that allows for the submission of a federal tax return is only applicable if the licensee is unable to produce financial statements. Subsection (a) states “A licensee shall prepare financial statements covering all financial activities...” Subsection (a), paragraph (4), subparagraph (A), also states “A Group IV licensee shall prepare financial statements...” The submission of federal tax forms for Group IV licensees only applies “if the licensee is unable to produce financial statements...” This is a current provision relating to what is now a subset of Group III (i.e., licensees with a gross revenue of less than \$500,000 per year), but has become Group IV under the proposed action. In other words, under the current regulation, a Group III licensee with gross revenue of less than \$500,000 per year that is unable to produce financial statements is permitted to submit a copy of a federal income tax return, as specified. Other than the creation of a new Group IV, there is no difference between the current regulation and the proposed action. Group IV licensees are those with gross revenue of less than \$500,000 per year.

According to the Final Statement of Reasons for the current regulation (CGCC-GCA-2003-02-R), this provision was included as a less expensive method of submitting financial information for those licensees with the lowest revenues. Business and Professions Code section 19840 provides that the Commission shall take into consideration the operational differences of large and small establishments to the extent appropriate. To delete the current provision permitting the submission of federal tax forms in limited circumstances would remove this less expensive and burdensome method and impose an adverse economic impact on those licensees who may be the least likely to have the resources necessary to hire an accountant.

⁶ Referring to the letter dated June 16, 2014, from Nathan DaValle, Assistant Bureau Chief, Bureau of Gambling Control.

In a review of this matter, no requirement could be found for the use of financial statements in the preparation of federal or state tax returns. In some instances, licensees' tax returns may be clearer and more concise than the supporting documentation used to prepare them. Furthermore, that supporting documentation is available to the Bureau for audit just as it is to the IRS.

- b. Tony York, Bureau of Gambling Control:** As auditors we will adapt if we have to, but the concern is that it will take the burden off the applicant and put it on the Bureau. Using the shoe box method of accounting, we would go ahead and collect those receipts and put those numbers together; but then it's our numbers and not the licensee's numbers. The issue with "in lieu of" is you're giving them that option. At this time, we haven't had to do this, but there is one cardroom that we're having issues with where we're probably going to have to go in and take their records and create financials if they can't do it themselves. We would rather have language where if you have the financial statements, submit those. But if you do not have them, then we would go ahead and accept the tax returns.

Response: This comment was considered, but was rejected. Again, this is a current regulatory provision. Section 12403 currently provides for the submission of a federal tax return only if the licensee is unable to produce financial statements. [See comments I.C.1.a. and II.B.1.a., above] This is precisely what Mr. York seems to suggest the requirement should be.

This proposed action does not affect the burden of preparation of financial statements or shift any burden to the Bureau. Again, this is a current regulatory provision. If a licensee is unable to prepare its own financial statements, and the Bureau wishes to perform an audit, the Bureau would currently have to use the licensee's receipts and other source documents to construct whatever records the Bureau auditors feel are necessary. The numbers would not be the Bureau's numbers since everything would have to be based on the licensee's receipts and source documents. Nothing is changed under the proposed action.

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

The current Section 12404 is renumbered as Section 12315, with amendments.

1. Subsection (b) – This subsection is amended to refer to Chapter X of Title 31 of the Code of Federal Regulations.
 - a. **Mr. Fried:** I think anytime you're writing regulations and you're referring to federal statutes and regulations, all of which evolve, to refer to them in a very specific way is a mistake, because when they evolve your references then are incorrect. It is better to just say, for subsection (b) and beyond, that we will comply and keep records available for inspection consistent with federal law on banking transactions, or consistent with FinCEN. If FinCEN changes, then you're going to have to come back and change the regulation.

Section 19841 of the Business and Professions Code doesn't require you to adopt this regulation. It says that the Commission is supposed to have regulations requiring us to keep records of cash and credit transactions. The regulations may include that we file reports with the department similar to what we file with the federal government on cash transactions. However, that's not what the regulation does. It just says that we have to have the reports on the premises and available for inspection. I don't think you have to require us to do anything except comply with federal law and have those compliance records available for inspection.

The practice is you fill out the [federal] form and it's filed electronically, then you print a copy and put it in your file. And that form may change, you know, two months from now. They may make a change in the form of what they're looking for. We don't need duplication. Because tomorrow, if they amend FinCEN, they may change the section number and then you're back here having to amend a regulation just to modify a section number.

We don't need to include a sentence in (b) saying we have to comply with federal law. We have to comply with federal law whether it's in this regulation or not. But in (c) we could say, "A gambling enterprise, regardless of gross revenue, shall make and keep on file at the gambling establishment a report of each transaction in currency in excess of \$10,000, as is required by federal law." And then keep the next sentence, "These reports shall be available for inspection at any time as requested by the Bureau." And then get rid of the next sentence and all the subparts.

Response: This comment was accepted, and the proposed action was modified as follows to accommodate it:

“(b) A gambling enterprise, regardless of gross revenue, shall make and keep on file at the gambling establishment a report of each transaction in currency, in accordance with sections 5313 and 5314 of Title 31 of the United States Code and with Chapter X of Title 31 of the Code of Federal Regulations, and any successor provisions. These reports shall be available for inspection at any time as requested by the Bureau.”

Subsections (b) and (c) are consolidated in a new subsection (b) and subsection (d) is renumbered (c).

The phrase “and any successor provisions,” which is also used in both Business and Professions Code section 19841 and Penal Code section 14162, will address the applicability of any future changes in federal statute or regulation. All this subsection requires is that licensees retain copies of the applicable Title 31 reports – as they are already required to do – and make them available to the Bureau for inspection upon request.

There were no further comments received, either in writing or orally, at the July 23, 2014 public hearing.

III. 15-DAY CHANGE WRITTEN COMMENT PERIOD

The following written comments/objections/recommendations were received regarding the modified text of the proposed action during the 15-day written comment period that commenced August 11, 2014 and ended August 26, 2014:

A. 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, provisions such as allowing electronic communication and storage are repetitively added to individual chapters of the regulations as they are not yet generally allowed. These repetitive provisions are included in a general requirements section for simplicity and clarity. Duplications of these provisions are removed accordingly.

1. Subsection (c) – The current requirement of Section 12405 that each licensee must provide the Bureau with copies of any records upon request is 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. This maintains efficient and consistent procedures for the Bureau to obtain records for investigatory and auditing purposes.

a. Charles Bates, Bay 101, in an e-mail received August 26, 2014 (Mr. Bates):

Bay 101 suggests that the wording of the last line of 12003 (c) be modified to allow production of records on electronic media. If the Commission or the Bureau is unable to read or make a hard copy of the file then they could go back to the licensee and request a hard copy of the specific document or file that they need. This particular requirement by the proposed regulation is burdensome, expensive, time consuming and the SOR [statement of reasons] implies that electronic production is the preferred method. In light of today’s electronic media, hard copy requests are outdated. Requests made for documents by the Bureau or the Commission should be transmitted electronically, or by hard copy, whichever is most convenient and efficient. Considering the allowance in subparagraph (d), this sentence in (c) is confusing and contradictive. The last sentence in (c) is better deleted and the requirement of (d) adopted.

Response: This comment is not germane to the modified text of the proposed action. No modifications were made in subsection (c) of Section 12003 in the modified text published on August 11, 2014.

2. Subsection (d) – The option to store and submit records in either a permanent form or other media unless otherwise specified is added. As electronic methods of storage and communication become more common for licensees and the Bureau, this option would allow for faster and less expensive methods of communication and document storage.

a. Mr. Bates: Is the word “permanent” being used to mean “hard copy” or is it being used to indicate the many forms of permanent information storage –

electronic, paper, magnetic tape, CDs, thumb drives, ink, etc.? As described in the statement of reasons the intent appears to indicate primarily electronic media and alternatives to “hard copy.” This sentence needs to be clearer by clearly stating that the preferred method for transfer of documents and response to requests for documents is electronic media. Additionally, this subsection seems to negate the need for the last sentence in 12003(c), as discussed above.

Response: This comment is not germane to the modified text of the proposed action. No modifications were made in subsection (d) of Section 12003 in the modified text published on August 11, 2014.

B. Section 12311 – Definitions.

The current Section 12400 is renumbered as Section 12311, with some amendments for accuracy and clarity. The meaning of the words and terms in this article may not be consistent with the meaning of similar words or terms used in other existing regulations. As a result, these definitions are necessary to ensure that the proposed regulations are clear, concise and easy to understand.

1. Subsection (a) – The current subsection (a) of Section 12400 is retained in Section 12311 and amended to reference the definitions in Section 12002.

a. Mr. Bates: Section 12002 of the B&P code relates to Food and Agriculture. What section of the B&P code is being referenced? Perhaps, this is a typo and it should read “and Section 12002 of this division.”

Response: This comment is not germane to the modified text of the proposed action. No modifications were made in subsection (a) of Section 12311 in the modified text published on August 11, 2014. While this comment is not germane, a nonsubstantive, grammatical change to this subsection is made for clarity and to be consistent with the original intent. This change adds clarifying language that does not change the meaning of this subsection. The subsection is changed to read as follows:

“(a) Except as otherwise provided in subsection (b), the definitions in Business and Professions Code section 19805 and Section 12002 of this division shall govern the construction of this chapter.”

The addition of the phrase “of this division” clarifies that the reference is to Section 12002 of Division 18 of Title 4 of the California Code of Regulations, and not section 12002 of the Business and Professions Code. Adding this language is a nonsubstantive grammatical, editorial change that has no regulatory effect.

C. Section 12313 – Financial Statements and Reporting Requirements.

The current Section 12403 is renumbered as Section 12313 with non-substantive edits for clarity and simplicity.

1. Subsection (a) – The current reporting requirements of Section 12403 are amended to include TPPPS companies and gambling businesses. The various license types are specified for clarity. TPPPS companies and gambling businesses will have different information to submit on their annual financials than gambling enterprises due to the different natures of the entities. Therefore, the license types are individually referenced rather than trying to refer to them collectively as “licensees.”
 - a. **Mr. Bates:** This Licensee does not have access to the information required by this sentence, nor does it seek such information on the TPPPS company. It is presumed that the TPPPS would also reject any requirement to share “all financial activities” with this licensee. Bay 101 believes this requirement is unclear, confusing, invasive, unreasonable and burdensome. Additionally, it would cause undue acrimony between the participants in the business operation if the financial activities of one party was ordered given to the competitor or adversary. This requirement is unreasonable and should be either dropped or reworded to clearly require the TPPPS to abide by this article, which seems to be the intent indicated in the SOR published by the regulator. It should not require the licensee to prepare a financial statement on “all activities of the TPPPS company.”

Response: This comment is not germane to the modified text of the proposed action. No modifications were made in subsection (a) of Section 12313 in the modified text published August 11, 2014.

While this comment is not germane, a nonsubstantive, grammatical change to this subsection was made for clarity and to be consistent with the original intent. This change added clarifying language that does not change the meaning of this subsection. The subsection was changed to read as follows:

“(a) Each licensee shall prepare financial statements covering all the financial activities of the TPPPS company, the gambling business, or the gambling enterprise, as applicable, for each fiscal year, in accordance with generally accepted accounting principles, unless otherwise provided in this section.”

As used in Chapter 5, the term “licensee” includes owner licensees, as defined in subdivision (ad) of section 19805 of the Business and Professions Code, as well as holders of TPPPS or gambling business licenses or registrations. Clearly, the intent of subsection (a) of Section 12313 is to apply the requirement to prepare financial statements to all three license types. The addition of the phrase “as applicable” clarifies that the requirement applies to financial statements for the financial activities of the particular licensee. Adding this language is a nonsubstantive grammatical, editorial change that has no regulatory effect.

2. Subsection (a), paragraph (4) – The reference to those in Group III with gross revenue of less than \$500,000 per year is changed to refer to a new Group IV.

- a. **Mr. DaValle:** Mr. DaValle reiterated the Bureau’s previous comment concerning the option to submit a federal tax return in lieu of financial statements. [See comments I.C.1.a. and II.B.1.a. and b., above]

Response: This comment is not germane to the modified text of the proposed action. No modifications were made in paragraph (4) of subsection (a) of Section 12313 in the modified text published August 11, 2014.

3. Subsection (b) – The repetitive provisions in paragraphs (2), (3), and (4) of subsection (a) of Section 12403 are consolidated and merged into subsection (b) of Section 12313 for simplicity and clarity.

- a. **Mr. Bates:** This paragraph seems to be inconsiderate of the licensee’s constitutional rights to due process. Mere “concern” about the laundry list of areas which someone may have reviewed or analyzed is insufficient to grant the Bureau sweeping power to order significant monetary expenditure by a licensee. This may amount to a “taking.” Any order of this nature should be sparingly used and ordered, after due consideration, review and decision by the Commission. To allow the Bureau to order a licensee to incur such financial burden without due process is not within their power nor can it be granted by regulation. This section should clearly state that such order may only be made after a “finding” by the Commission.

Response: This comment is not germane to the modified text of the proposed action. No modifications were made in subsection (b) of Section 12313 in the modified text published August 11, 2014.

4. Subsection (e) – The current subsection allows the Bureau or the Commission to require a licensee to engage an independent accountant, as specified, to perform a fraud audit if fraud or illegal acts are suspected. The phrase “by the Bureau or Commission” is added at the end of the subsection as a nonsubstantive change to clarify by whom the fraud or illegal acts are suspected.

- a. **Mr. Bates:** If there is a “suspicion of fraud or illegal acts,” the licensee must be afforded due process. Neither the Bureau nor the Commission has the power to order the licensee to waive its 5th amendment right. The bar is raised when the words “illegal activity and fraud” are bandied about. If there is suspicion that fraud or illegal activities are afoot then the investigative entity must use the tools available to it via the criminal procedure. It cannot use its administrative position to force a citizen to investigate itself for the benefit of the investigator and the detriment of self. This paragraph must be adjusted to provide for due process protection of the licensee or be deleted in its entirety.

Response: This comment is not germane to the modified text of the proposed action. This comment is directed at the provisions of this subsection in general and does not relate to the specific nonsubstantive clarifying change that was

made. The provisions to which this comment pertains are part of a current regulation (subsection (d) of Section 12403) that is being renumbered as subsection (e) of Section 12313, without any substantive change. The only change being made is the addition of the phrase “by the Bureau or Commission” at the end of the subsection to clarify by whom the fraud or illegal acts are suspected.

There were no further comments received within the 15-day change written comment period regarding the modifications to the proposed action.

IV. COMMENT RECEIVED OUTSIDE THE PUBLIC COMMENT PERIODS

The comment letter listed below was not received during any of the abovementioned public comment periods. While it is included in the rulemaking file, it has not been summarized or responded to.

1. Letter dated July 21, 2014, from Mark Kelegian, representing the Oceans 11 Casino and the Crystal Casino.

There were no further public comments, objections, or recommendations received regarding the proposed action, either within or outside any of the public comment periods.