LAW OFFICES OF DAVID M. FRIED

6 Beach Rd., # 1115
Tiburon, CA 94920

Phone: (415) 370-0929
Fax: (415) 360-5289

December 1, 2022

Chairperson Paula D. LaBrie
Commissioners Eric C. Heins, Edward Yee, Cathleen Galgiani, William Liu
Gambling Control Commission
2399 GATEWAY OAKS DR. STE 220
SACRAMENTO, CA 95833-4231

Re: Proposed Transaction Regulations

Dear Chairperson LaBrie and Members of the Commission:

On behalf of the Oaks Card Club and California Grand Casino, we support the goals of improving disclosure and oversight of transactions. We also appreciate that these are complex and difficult regulations to write, including choices about how to define terms and what mandatory duties to impose. Nonetheless, before the formal A.P.A. process begins, the regulations should be revised to be more sharply focused, which can be done without compromising the Commission's regulatory aims.

For example, because the proposed definitions of "affiliate" and "transaction" are deliberately broad, the substantive requirements using these definitions can be overbroad. The Gambling Control Act §19805(a) defines an affiliate as someone controlled by a specified person. The proposed definition of "affiliate" in this regulation abandons the notion of control. As a result, the regulation would impose mandatory duties on persons and entities neither under the Commission's jurisdiction nor under the control of a licensee.

The regulation often imposes requirements on "licensees," or "owner category licensees." The former includes key employees and the latter includes all individuals endorsed on a license. Yet many of the requirements are more appropriately tailored to the operating businesses, that is, the "Cardroom business" or "TPPPS business" licensees.

Because of issues like this, the regulation creates significant and i some cases unnecessary record keeping and reporting requirements. After the regulation was last considered at a workshop in 2018, the Commission conducted a survey to determine the regulation's impacts, but the data was not compiled and the Commission is being asked to move forward without that data. We are also unsure if the Bureau has estimated its expected costs to implement this regulation. In addition, other comments from the 2018 workshop have not been incorporated.

The Commission has to identify its objectives for this regulation, and then conform this regulation to those objectives in a reasonable way.

Comments by Section

I. Definitions

A. Affiliate. §12002(d)

The definition of "affiliate" in §12002 is much broader than the Gambling Control Act's definition. Section 19805(a) defines an "affiliate" as someone under the control of a specified person.[1] The proposed regulatory definition lacks the element of control and explicitly includes many other unlicensed persons.

Subsection (2) of the proposed definition of "affiliate" states that when a person that is licensed (or specified) has an investment in another business, the unrelated persons involved in that other business or investment are "affiliates." For example, if a licensee owns 10% of a beverage distribution business, or a real estate limited partnership that owns real property that is rented, under subsection (2) the directors, officers, general partner, managing member, general partner or person in control of that beverage distribution business or real estate partnership would be defined as the licensee's affiliate even though their association has nothing to do with gambling, and even though the licensee has no control over these other persons.

Similarly, subsections (3), (4) and (5) of the definition includes spouses, some family members, even some in-laws, sister and brother in laws, and trusts and estates even where the licensed person is not the trustee but merely a beneficiary of the trust. So if I am licensed and my spouse is a beneficiary of a trust set up by her great aunt before our marriage, that trust and trustee are now *my* affiliates.

The Commission has no jurisdiction to impose mandatory conditions on these other persons yet three sections of the regulation, §12311.2(h), § 12326(f), and § 12326(g), would do so.

Perhaps the reason for proposing a broad definition of "affiliate" is so that under 12324(c)(6), this broader group of persons or entities would be included in the reportable summary of each transaction. But the regulation's use of this same broad definition throughout the regulation is a mistake because often in the other sections where the term is used the scope is too broad.

As an alternative, the regulation should use the definition of "affiliate" in the Act. If the Commission wants the reporting requirements imposed on the licensees in §12324(c)(6) to refer

[1] Gambling Control Act §19805(a) "Affiliate means a person who, directly or indirectly, through one or more intermediaries, controls, is controlled by, or is under common control with, a specified person."

to other persons that don't meet the statutory definition of "affiliate" from the Act, then the reporting requirement in §12324 (c)(6) can be written that way.

Another reason for using the Act's definition is that this proposed regulation would put the definition of "affiliate" into the general definitions for all Commission regulations. This may impact other regulations considered in the future. For this reason as well, it would be better to use the same definition of "affiliate" as used in the Act as the default definition for Commission regulations generally and to refer to other persons only when needed for individual requirements, like reporting. Consistency between definitions in the Act and the Commission's general regulatory definitions will avoid confusion.

B. Transaction. §12311(a)(8)

The definition of transaction is also broad, although in the substantive provisions that follow in this regulation the over breadth can be addressed without a wholesale change to the proposed definition. For example, establishing a dollar threshold for transactions for both record-keeping and reporting would reduce the issue of over breadth caused by an expansive definition of transaction.

That said, there are two specific changes that should be made to the definition.

1. The definition of "transaction" carves out the *"one-time purchase of goods unless the purchase includes a warranty beyond that of implied merchantability."* Under this definition, if the purchaser receives a *written* warranty, for example a two year written warranty on a new copy machine, then the carve out for the one time purchase of goods does not apply. This distinction between *express and implied* product warranties does not serve a regulatory purpose.

We suggest that the warranty reference be dropped all together so that one time purchases of goods are excluded, or that the exclusion include all warranties, express or implied.

2. The reference to the "transfer or assignment of an interest through a gift" can be narrowed. For example cardrooms donate to non-profits used playing cards, expiring food, old equipment and furniture, etc... all of which transfer ownership of the item. When cardrooms closed the tents in which many operated during COVID restrictions, some cardrooms gave away much of the equipment and furnishings to local non profits. In addition, individual owners and key employees may also donate business property. They might donate property to a non-profit or give it to a family member. It is not clear what the regulatory interest is in tracking gifts to non-profits or to family members, especially those of lesser value. The regulation instead should refer to the transfer of an ownership interest in an owner category license, that is, an interest in a cardroom or TPPPS owner or endorsee, unless including gifts has a different objective. Establishing a monetary threshold for transactions for record-keeping and reporting would also help.

This should be narrowed to refer to "transfer or assignment through gift or otherwise of an ownership or profit interest in an owner category licensee ~~through a gift~~."

II. Recordkeeping. §12311.2 (a).

(a) A licensee must maintain all documents such as contracts, invoices, purchase orders, receipts, purchase correspondence, or confirmations, which document the transaction.

The record keeping requirement is too broad with regard to: (1) the scope of transactions for added record keeping, (2) the type of documents licensees would have to keep, and (3) the persons who have to keep records. In addition, the regulation should permit records to be kept in digital form.

First, the record keeping requirement applies to all "transactions" broadly defined. Yet the universe of transactions that require Commission pre-approval is narrow and the universe of transactions subject to reporting has several exceptions.

There is no substantial reason to keep "all documents" for seven years for transactions that are neither reportable to the Bureau nor require the Commission's pre-approval. The definition of "transaction" in §12311(a)(8) is broader than the reporting requirements under §12324. Yet, the record retention provision, § 12311.2(a), refers only to the broad definition and is not limited to reportable transactions or transactions requiring pre-approval.[2]

Second, maintaining *"all documents such as contracts, invoices, purchase orders,*

[2] Cardroom and TPPPS business licensees already have an obligation to maintain specified records for all expenses and transactions under existing Regulation 12312(b), which will cover the transactions that do not have to be reported under the proposed §12324, but without having to keep "all documents" for these other non reportable transactions. Regulation 12312(b) now provides:

Each licensee must:

(a) Maintain all records required by this article for a minimum of seven years.

(b) Maintain accurate, complete, and legible records of all transactions pertaining to financial activities. Records must be maintained in sufficient detail to support the amount of revenue reported to the Bureau in renewal applications.

(c) Maintain accounting records identifying the following, as applicable:

(1) Revenues, expenses, assets, liabilities, and equity for the cardroom business licensee or TPPPS business licensee. ...

receipts, purchase correspondence, or confirmations, which document the transaction," includes all emails, texts, handwritten notes and perhaps other redundant records. There are often dozens or hundreds of emails or texts in the course of the negotiation or performance of a single contract that have nothing to do with establishing the elements of the transaction that are being reported to or reviewed by the Bureau. This problem is magnified because the definition of "transaction" will broadly sweep in thousands of transactions.

Many emails or texts may involve simple items such as simply scheduling a telephone call, a delivery or site visit, asking questions, tracking a product, or emails proposing different services or goods options, etc.... There are countless emails or texts regarding maintenance issues or food service under on-going transactions or contracts. The head of facilities or maintenance or head of food and beverage could each have thousands of texts and emails a year that relate to the performance of contracts or services.

Collecting and preserving all these records, especially texts between dozens of employees or between employees and third parties, or handwritten notes or other supplementary records, is very difficult for any business or individual. Because many employees use personal cell phones with just a monthly reimbursement from their employers, the task is even harder. Maintaining these duplicative and irrelevant records for seven years is also unnecessary.

Third, the proposed record keeping requirement applies to all "licensees" even thought the reporting requirement in section 12324 only applies to "owner category licensees." There is no justification for keeping records for seven years for transactions that are not reported, and by people who don't have to report transactions. Moreover, if key employees and endorsees are swept into a record keeping requirement for all "transactions," it should only be for something they are required to do, for example for those transactions requiring Commission approval.

Fourth, this section should allow for transaction records to be kept in digital form, provided the records are accessible, rather than requiring licensees to keep multiple copies in electronic and printed form. The phrase "all documents" may suggest that we have to keep anything and everything and in both digital and printed form once a document or record is created.

To address each of these problems, this section should be modified as follows:

(a) A cardroom business licensee and TPPPS business licensee must maintain ~~all~~ documents ~~such as~~ with the information required to be reported under section 12324(c) (1)-(7) including contracts, invoices, purchase orders, and receipts~~, purchase correspondence , or confirmations, which document the transaction~~. Licensees also must keep all documents relating to the terms of a transaction subject to Commission approval under section 12326. The records required by this section may be kept in digital form if the digital records are

readily accessible. Licensees are not required to keep documents regarding service calls or relating to the performance of a contract or agreement unless the records evidence a modification to the parties agreement, their rights or obligations.

III. Access to Records by other Agencies. §12311.2 (b).

This section requires that any records of transactions have to be provided to any government law enforcement agency or federal, state or local regulator, if working with the Bureau "on the specific topic or area cited in the request."

There are several problems with this section.

First, all agencies have some limits on their authority, *and processes they have to follow* in requesting information or, as appropriate, issuing administrative subpoenas. This is true of the Bureau as well. Section 19827(a)(2) of the Act requires the Bureau to obtain administrative subpoenas or warrants in some cases. (Generally, the Bureau would use an inspection warrant for locations other than the gambling establishment.)

In contrast, under this regulation other agencies could request documents from *any licensee* with nothing more than an email or text message which qualify as "writings." *See* Cal. Evid Code §250. This section would eliminate the need for other agencies to follow their own agency law and process for obtaining records so long as the Bureau stated that the two agencies were working in conjunction on a specific topic or area. This is even more lax than the limitations on the Bureau under §19827. Section 19827 not only sometimes requires a warrant, but where it does not, it does so only with reference to the gambling establishment. In contrast, this proposed section applies to all licensees, including endorsed persons and key employees, and without regard to location.

While most licensees are willing to cooperate informally with law enforcement on any occasion, compelling cooperation under the loose standards of this section is inappropriate. Agencies that request records from a business or individuals have to follow a well defined and formal process for doing so, found in state law and sometimes contained in their own agency regulations. These laws and regulations specify a time for response, for hearing objections, and for protecting the rights of third parties where appropriate, etc… The laws and regulations may require a subpoena rather than a written request. If the ABC, ATF, IRS, Colorado Labor Commissioner, Montana Fish and Game Bureau, etc… wants to request records, they have established procedures they must follow with any person, taxpayer or license holder. Depending on the request, its scope and purpose, and the implications on the rights of third parties, a licensee may want to invoke these administrative protections when needed. There is no compelling reason for upending the legal processes used by other agencies and allowing them to get any records they want with nothing more than a letter, email or text.

Moreover, applying this process to records maintained by any licensee, including individuals, and without regard to the location of the records, may be unprecedented.

Second, the proposal is not limited to agencies working with the Bureau *on a particular investigation.* Rather, the language permits other agencies to make requests so long as the "topic" or "area" is the same, suggesting that even research requests without a focus on a specific licensee is permitted and the response obligatory. [3]

Third, the Bureau may have a reason to ask for information for licensing purposes, but the other agencies included in this regulation do not have the same interest in licensing. If the investigation by the other agency is for a criminal matter or can lead to criminal charges, this process violates the Fourth and Fifth Amendments by requiring an individual or business to unwillingly provide records to an agency other than the Bureau without a subpoena and with the risk of disciplinary action for violating a Commission regulation.

Fourth, some aspects of this provision are outside the scope of Commission authority. To the extent this new informal process applies to the Bureau's own requests for information, the Commission cannot adopt a regulation in conflict with section 19827(a)(2) which in some cases requires an inspection warrant.

In addition, the Act does not authorize the Commission to establish inspection rights for other agencies. Because the provisions in the Act that govern inspections are specific to the Bureau and Commission processes and do not include other agencies, the Act cannot be construed to include standards for other agencies or the ability by regulation to set inspection standards for other agencies. *See, Naidu v. Superior Court,* (2018) 20 Cal.App.5th 300, 307 (citing *Gray v. Superior Court,* (2005) 125 Cal.App.4th 629).

For these reasons, at the July 11, 2018 workshop on these regulations the Commissioners endorsed having all requests originating with other agencies to go through the Bureau, who would make the request to a licensee. (Hearing Time stamp 17.00 - 22:00 minutes). That was not implemented in this iteration of the regulations.

As a result, subsection (b) (2) should be deleted rather than amended. In addition, at the 2018 workshop, the Commissioners endorsed the idea that the administrative record for this regulation should reflect that the regulation is not intended to expand the types of documents or records that the Bureau can request.

IV. Confidentiality Agreements. §12311.2 (h).

This section provides that licensee and affiliates cannot enter into confidentiality

[3] The regulation is also not confined to domestic public law enforcement agencies. As written, this regulation would authorize foreign governments and tribal agencies to make written demands if working "in conjunction" with the Bureau on a "specific topic area."

agreements with third parties regardless of the subject matter or identity of the third party, if the agreement limits contact with government agencies.

This is one of three instances where the regulation mistakenly would impose mandatory duties on affiliates who are not under the jurisdiction of the Commission, and over whom the Commission has no regulatory authority. (*See,* §12311.2(h), § 12326(f), § 12326(g)). This provision has to be limited to contracts or agreements where the licensee is a party, and/or use the definition of affiliate in the Act.

For example, if I am a licensee, the Commission has no jurisdiction to order the trustee of my wife's aunt's trust to include or not include certain terms in all the trust's contracts with other parties where neither party to those contracts is a licensee or under the jurisdiction of the Commission. My wife cannot change the terms of her aunt's trust, cannot order the trustee to include specified terms in all the trust's contracts, and should not have to disclaim her beneficiary interest in her aunt's trust so that I can be licensed. Nor can the licensee, the sole person over whom the Commission has authority, order their spouse or trustee to do any of these things. Similarly, the Commission cannot adopt regulations on a person who is the manager of the beverage distribution business or real estate partnership telling such a person what they can and cannot do in all their business contracts because a licensee invests in that business.

In addition, even where a licensee is a party to the agreement, this provision should not exclude notice to the other contracting party that the information has been requested by a government agency: a very common contract term that requires notice to the other contracting party before information is provided to an agency. [4]

We suggest simplifying this section as follows:

> *No licensee , ~~nor any of their affiliates~~ may enter into, or cause any other ~~person~~ licensee or affiliate as defined in section 19805(a) of the Act, to enter into, any agreement that limits contact with or restricts information that can be provided to officials or employees of the Commission, the Bureau, the Department of Justice, or any federal, state or local agency with applicable enforcement or licensing authority over gambling or gaming activity. This does not limit an agreement that the party receiving the information request notify the other party to the transaction of the request before the information is disclosed.*

[4] There are many legitimate reasons for confidentiality provisions; for example, keeping private information such as pricing, trade secrets, new products, client lists, marketing strategy, and other information. The agreements may not prevent disclosure to government agencies, but may within the terms of the regulation "limit contact with" agencies by requiring the party receiving the request to notify the other party before the disclosure is made in case the other party wants to object.

V. General Requirements. §12322

(e). Leases and Landlords. This provision would require landlords to contractually agree to assist tenant licensees in complying with all requirements of the Act, Commission regulations and Bureau regulations to the extent any requirements relate to a lease between them.

This overbroad provision could interfere with ordinary business and personal transactions.

- A "licensee" means anyone licensed by the Commission, even a key employee or endorsee. But the landlords of key employees and individual owners are not subject to regulation or even mentioned in the Act.

- This provision includes residential leases as well as commercial ones.

- This provision does not just apply to a gambling facility, but also applies to a TPPPS or licensee renting office space in a standard office building.

(Absurd as it may sound, as written this regulation applies to an apartment lease by a key employee, which is obviously is not what is intended.)

Even for commercial leases of the gambling facility, the vast majority of landlords don't know what the Gambling Control Act or agency regulations require, and may not undertake uncertain commitments like this. The exception may be landlords leasing large specialty facilities used for cardrooms and only to the extent they know exactly what they are agreeing to. But this regulation is not currently limited to leases of the gambling establishment, or even leases with the cardroom business licensee. And even if so limited, the regulation should more clearly state for landlords which sections of the regulations the landlords need to know.

Even if limited to the gambling establishment buildings, smaller cardrooms may occupy non specific spaces, such as in a strip mall. The standard lease forms for general commercial space provide for certainty in the Landlords' obligations. Those forms usually provide that is the tenant's responsibility to comply with all applicable laws. Commercial landlords often just deliver a shell and warrant the building complies with building and ADA codes.[5] Everything else is the responsibility of the tenant. Landlords do not undertake legal obligations to assist tenants in complying with laws the landlords have never encountered before and framed by open ended references the landlords do not readily understand. This means that licensees will be restricted in what property they can lease.

If the sole reason for this provision is for landlords to cooperate with the gambling

[5] *See, e.g.,* Section 2.3, AIRCE Single Tenant Lease 2017, STN-27.10, rev. 11-1-2017.

establishment tenant on security issues, the provision could be written in a different way:

> *(e) Any lease between a cardroom business licensee and a landlord for the gambling establishment must contain an acknowledgment that the landlord ~~is familiar with~~ has been provided with a copy of ~~subsection (d) of Section 12326(d)~~, the security and surveillance requirements in sections 12395 and 12396 of these Regulations and will assist the licensee with complying with these regulations. Nothing in this section requires that the Landlord pay for the costs of complying with sections 12395 and 12396.~~ ~~the requirements of the Act, Commission regulations, and Bureau regulations, to the extent any requirements are triggered by, or result from, the lease.~~*

(g) For any transaction requiring pre-approval, this provision prohibits any activity under a contract until the Commission has approved it.

Often real estate sale or business sale contracts require obligations upon execution of the agreement and prior to closing, none of which offends the Commission's regulatory interests in making sure the buyer is licensed before operating or profiting from the business.

For example, the contract may require the buyer to pay a good faith deposit, conduct due diligence, waive initial or some final conditions to sale, and keep the price confidential. The seller may be required to maintain the business without material change until the sale closes, for example keeping the business's existing licenses, staff, lease, marketing and service contracts pending closing, train the prospective buyer, etc... This list is not exhaustive, and the regulation should permit other actions to be approved by the Commission on a case by case basis.

This section should be modified as follows:

(g) All transactions requiring prior approval pursuant to this article cannot specify a closing date, or include any provision that allows for any party to the transaction to ~~perform any duty or obligation,~~ confer any material benefit, or receive any ~~right,~~ material benefit, ~~service, privilege,~~ compensation, interest, or assignment of interest prior to the approval of the transaction by the Commission, except for good faith deposits, or as approved by the Commission upon the request of one or more of the parties.

In addition, there is overlap between this section and the first paragraph of section 12326. The two sections should be consolidated to avoid inconsistency.

VII. Reporting Requirements. §12324

A. We recommended in 2018 that there be a monetary threshold for the reporting of transactions, which the Commissioners agreed should be examined. (Time stamp - 58:46-

1.03:30). But a threshold was omitted from this draft.

Previously, the Commission sent a survey to business licensees to assess the impacts of the regulation. The survey asked for a list of individual transactions, the name of the vendor and the aggregate value of each reported transaction. This information would be useful to now know because it would show the impact of including a dollar threshold for transaction reporting and for excluding certain types of transactions. This is so even though this draft of the regulation did exclude a few types of transactions based on the Commissioners input in 2018: government payments, insurance, utilities and payments to publicly traded companies. The survey would nonetheless show how many annual transactions there were over any particular dollar threshold.

Here is why a dollar threshold is needed.

- Suppose a card room hires 14 people to appear in an advertising photo and video shoot. The shoot takes half a day. They each receive $100 and sign a publicity waiver. Their booking agent receives $400 and also signs a contract. The card room hires a photographer for $750 with an invoice with terms and conditions including that the cardroom owns the photos. A make-up person receives $200 and undertakes the obligation to be on site for four hours. The video production company charges $5,000 and has a contract. There are no other transactions with any of these persons in the same year. (This is a real world event.)

- These activities are transactions: they involve the provision of services and the modification of rights and obligations where monies are exchanged. Seventeen of the 18 people referenced actually sign agreements with legal duties.

- Under subsection (c), for each of these 18 people and 18 transactions, the card room has to report the dates of work, their names, the purpose of each transaction; a description of the goods and services, and a summary of the rights and duties – meaning a summary of the booking, publicity, production and photography agreements.

- Under (c)(6) the card room also has to list *all affiliates* The definition of affiliate is the broad one proposed for the regulation. Assuming (c)(6) refers to the 18 persons who are parties to these various agreements, it is unreasonable to expect each of these 18 persons or companies – many of whom are only paid $100 -- to identify any family member or partner that lives with them, any person who controls any investments or businesses in which they have an ownership interest, and any trust in which they or a spouse or registered partner are a beneficiary … all because they were paid for a half day photo shoot. Not one of these 18 people is going to do this.

This is not only a problem in dealing with individuals that provide services, but also large non-publicly traded companies who have hundreds of clients and whose management may well

balk at these requirements.

Cardrooms have a lot of service contracts not just for marketing, but for food service or facility work, for example plumbers, landscapers, engineers, facility and equipment repairs, the installation of goods, carpentry, etc... We may make incidental purchases of gaming related goods, like plastic chip trays, table felts or chairs. A Tier III cardroom might have 200 - 300 reportable transactions in a year under this regulation. In addition, a licensee may use credit cards for some transactions. So even if there is one vendor – Visa – each monthly card statement may contain another 25-50 transactions. Even if each vendor is assumed to be one transaction, without a dollar threshold these are horrendous numbers for compliance. Someone has to determine for each transaction whether it has to be reported (was the transaction for a good with only an implied warranty?), and then for reporting and tracking by the licensees and Bureau. This imposes a substantial compliance workload on licensees, many of whom have administrative employees already tasked with many other compliance tasks as well as the daily tasks of just running the business, hiring employees, scheduling employees, supervising games, ordering goods, arranging services, etc....

- The regulation also applies to all "owner category licensees" meaning that it sweeps in all the hundreds of individuals and trusts endorsed on a business license, with an ownership interest in a TPPPS or cardroom business, or an officer of either, or a trustee of any endorsee. This means that not only the cardrooms and TPPPS companies have to report all their contracts, but that all the individual owners will also be making these detailed annual reports about business contracts without regard to their percentage ownership interest.

With roughly 80 card rooms and a dozen or more TPPPS, plus hundreds of individual owners, trustees and officers, the regulations could contemplate the reporting and cataloging of thousands or tens of thousands of transactions industry wide. Much of that information would concern smaller transactions or transactions that by their nature are not suspect and which will never be reviewed. Having the licensees compile and the Bureau categorize background information for every transaction and then assign a unique number to each is a complete waste of time.

What is more, there is no regulatory justification for the reporting and cataloguing of hundreds or thousands of *de minimis* transactions. If there were, then surely other regulated industries in California and gaming regulators in other states would have similar rules requiring licensees to report nearly every transaction without regard to dollar amounts to the government and be assigned a unique identifying number for each. The regulatory compliance costs for the industry and all the individuals, and higher annual fees to compensate for the new Bureau's added workload and budget, could be horrendous. The regulation could avoid much of these costs by being more focused.

We suggest a reporting threshold of the lesser of $75,000 or 0.5% (one half of one percent) a year of the licensed business' gross revenues. This will scale the reporting to the size of the cardroom or TPPPS. Cardrooms or TPPPS with revenues under $15,000,000 will have a sliding scale while all others with $15 million or more in annual revenue will use the $75,000 threshold. The regulation should also raise the threshold by the rate of inflation.

With a dollar threshold, the number of transactions for an average Tier III cardroom could be 15 or fewer a year and proportionally more for larger cardrooms (although a survey would help estimate the number).

In addition, the regulation should be limited to the cardroom or TPPPS business licensees. If there is a need to include individual owners, it should be those that either have a controlling interest or manage the business.

If the regulation pares down the reporting, the Bureau can actually focus on transactions that may matter, instead of being tasked with reviewing and inputting every miscellaneous transaction, and tracking thousands of transactions in a database.

In addition, the Commission should consider that there are lower cost, higher reward alternative to micro-reporting, and which don't require new regulations. Under existing regulations card rooms have annual independent outside financial audits. These audits can be used to identify transactions by particular licensees that are disproportionate to the norm. So if the Commission is concerned that a transaction is hiding a payment that is really a share of card room profits or for some other purpose, then the audit can serve as a basis for further inquiry. For example, the Bureau could take the audited card room financial statements for recent years and develop industry averages for expense categories. If the usual expense for janitorial services or human resources consulting is less than 0.25% of operating expenses, a card room paying 2% is going to stand out. The Bureau can request additional information of those flagged transactions.

Not only would this alternative more effectively focus Bureau review, but it would spare the card rooms that are not engaging in unusual activity – *and the Bureau* -- from reviewing and assigning individual tracking numbers on tens of thousands of transactions.

We suggest the following changes:

(a) All transactions conducted by a cardroom business licenses or TPPPS business licensee (or an owner category licensee that manages or has a controlling interest in a business licensee), ~~an owner category licensee~~ that exceed the lesser of $75,000 or 0.5% (one half of one percent) a year of the licensed business' gross revenues must be reported annually to the Bureau. The $75,000 threshold shall be adjusted every three years by the average of the change in CPI for the Los Angeles, San Francisco and San Diego metro areas for the prior year.

B. There was a discussion in 2018 about excluding legal service contracts from

reporting. The Commissioners asked for legal authorities regarding whether such contracts should be excluded under section 12324(d).

Attorney-client communications are privileged. Cal. Evid. Code §952. The fact that a person sought advice on a particular subject is privileged, as would be the fact that they sought advice from a particular lawyer, as most attorneys have an area of practice which could reveal the subject matter of the consultation. *See Rosso & Ebersold v. Superior Court,* (1987) 191 Cal.App.3d 1514, 1519. The relationship with a named attorney should not be disclosed unless it has already been disclosed in public proceeding where the lawyer has appeared for the client.

The attorney – client fee agreement is also privileged under Business and Professions Code §6149. "A written fee contract shall be deemed to be a confidential communication within the meaning of subdivision (e) of Section 6068 and of Section 952 of the Evidence Code."

The Attorney-Client privilege is broader than the just the fee agreement; it covers all communications. It is unconditional and absolute. Even whether an attorney handed or mailed his client a public document to look at is privileged because it could reveal the subject matter of the discussion between them. *In re Navarro,* (1979), 93 Cal. App. 3d 325, 329. Disclosure of any communication cannot be ordered regardless of relevance or necessity even if that means some information is not acquired by another party or the government. *Shannon v. Superior Court*, (1990) 217 Cal.App.3d 986, 994-5.

Thus, the Commission cannot require the reporting called for in the regulation: a report of the contract's terms, including when it started, the names of the parties, purpose, and a description of the services and value exchanged.[6] Not only is the legal service contract protected but billing statements which describe the work performed are privileged. An agency cannot compel waiver of the privilege or advance consent to waive or limit the privilege as a condition of being licensed. "Waiver cannot be directly compelled [and] neither can it be indirectly compelled." (citation omitted)." *Regents of University of California v. Superior Court*, (2008) 165 Cal. App. 4th 672, 680-81; Cal. Evidence Code §912(a) ("without coercion"), §954.

In light of these authorities, the following should be added to the list of excluded contracts in section 12324(d)

> *(5) Transactions with attorneys covered by the attorney-client privilege. Attorneys and accountants also do not need to report their affiliates.*

Notably, the licensee's annual financial statements will show the aggregate amount paid for legal fees and professional services. Where appropriate the reporting party may name individual firms or lawyers without contract terms or specific amounts reported.

---

[6] It is not clear what "affiliates" would also have to be reported. Would the licensee have to identify the lawyer's law partners, co-habitants, child, grandchildren, or family trusts?

VIII. Pre-Approval Requirements. §12326

For the reasons above on page 10 (§12322(g)), the first sentence of this section should be changed as follows:

> *Licensees must submit the following transactions to the Bureau for review and must receive approval from the Commission before any party to the transaction ~~performs his , her or its duties or obligations,~~ confers any material benefit, or receives any ~~right,~~ power, material benefit, ~~service, privilege,~~ compensation, interest, or assignment of interest, except for good faith deposits, or as approved by the Commission upon the request of one or more of the parties.*

(a) This section requires pre-approval for *any* ownership interest in *any* gambling business. It would prohibit a licensee from buying a single share of stock in a publicly traded company that lawfully operates horse racing in California or a casino in other states.

There is no need for this provision.

- Owner licensees are prohibited from purchasing more than a 1% interest in gambling business that cannot legally operate in California. Gambling Control Act, §§19858; 19858.5. So Commission approval is not needed for purchases above the 1% threshold because such a purchase is prohibited.

- Nor is Commission approval needed for purchases of a business in any ownership degree that can legally operate in California. There is no prohibition on a licensee buying an entire horse racing track, or a single share of stock in one, if they wanted to do so, and no requirement that the Commission pre-approve it.

- So the only conceivable application of this section, to purchases of less than 1% of the stock of a company that operates gambling outside California that would not be legal in California, does not require individualized consideration and approval. Anyone that wants to buy 100 shares in public stock in a publicly traded company which operates casinos in other states should not have to file an application, pay fees, and wait 4 months for Commission approval.[7]

---

[7] In addition, the phrase "any business where gambling is involved" might sweep in some non obvious companies and activities because investments can be indirect, and because under state laws "gambling" is often not sharply defined or easily applied to new mediums. Stock mutual funds may buy stock in companies that are engaged in gambling. Do these examples require Commission pre-approval? Arguably, the individual is buying into the fund rather than the gaming company.

A more challenging example may be a company like Yahoo that operates online games with free to play tokens in addition to tokens for purchase, and may restrict participation in certain states due to gambling laws. Twitch just eliminated unlicensed gambling live streams but did not eliminate other

For these reasons, we suggest subsection (a) be deleted and replaced in a different section with a notice provision as follows:

> *"Any licensee that buys an interest of 10% or more in a business that derives 50% of more of its revenue from the operation of gambling shall provide notice to the Bureau and Commission of the purchase within 30 days of the transaction."*

(f) and (g) Section 19878 of the Act prohibits an owner licensee or an affiliate (as defined in the Act) from contracting with or employing a person denied a license. These proposed regulatory sections prohibit all licensees of any kind and their affiliates as broadly defined in the regulation from doing so. There are several problems with these sections.

(1) These restrictions are not limited to the types of "affiliates" defined in the Act, that is, persons *controlled* by the licensee. Rather, this regulation uses the much broader definition in these proposed regulations which sweeps in many people a licensee does not control. The Commission has no jurisdiction to impose mandatory requirements on these affiliates.

(2) There is no assembled list of the persons for a licensee to review to see who a licensee or affiliate cannot contract with. The licensees and affiliates would have to use a Google search of the Commission's website to find these names, and then read the minutes of the Commission meetings to find out if an application was withdrawn with prejudice, denied, etc... They also have to determine if a person with a common name is the same person as the one on the website. Any licensed business may contract with any number of persons or businesses a year for goods or services, in the dozens or hundreds. This unwieldy task is likely to lead to many errors or just flat out non compliance. In order to implement sub section (f) and subsection (g), the hundreds of licensees covered by this regulation will need a database of the covered persons we can check in order to comply with this requirement.

This requirement should be changed as follows:

> *(f) Any transaction agreement between a <u>an -owner</u> licensee, or an affiliate of <u>an owner-licensee-as defined in section 19805 of the Act,</u> and a person, or a person who is acting as an agent on behalf of a person, who has been denied a license by the Commission, has had a license suspended or revoked by the Commission, or within one year of the*

---

gambling content. https://www.cnbc.com/2022/09/21/twitch-announces-ban-on-unlicensed-gambling-livestreams-after-backlash-.html Viatical settlements for life insurance contracts when re-sold to investors without an insurable family interest or commodity futures trading which is often weather dependent were sometimes regarded as gambling, requiring state legislatures to carve them out from the definition of gambling in statute. *See,* 720 ILCS 5/28-1 (b) (Illinois); Tex. Stat. §47.01 (Texas)). Are these businesses "where gambling is involved"?

effective date has had an application for Commission approval withdrawn with prejudice and who has been identified by the Commission on an accessible list for the purposes of this section;

The same change should be made to (g).

(i) This section restricts any changes to the rights or obligations of the parties under an approved transaction.

This is problematic because many changes are simply not material to the Commission's regulatory purpose for approving the transaction. For example, changes to the closing date, the address where notice is sent, the cure period for a contract breach, changing the term of a note from 7 years to 5 years, changes to indemnity agreements, extending the contract by 6 months, changing the time for removal of contingencies, the geographic scope of a non compete provision, etc... the list is endless and each change will require a delay of several months. Imagine a contract has a closing date of 21 days after Commission approval, but for some reason the parties can't meet that date and need to amend that date after the approval. Do they have to wait four months? Or, the contract states that the buyer is assuming the seller's lease of kitchen equipment on closing, but the equipment breaks or the parties decide otherwise and the buyer won't assume that lease.

We suggest the following change:

(i) Any transaction that materially amends or modifies any transaction previously approved by the Commission. An amendment is considered material if the amendment grants, denies, expands, or diminishes any rights or obligations under the transaction by changing the financial consideration, source of funds used, or benefits to a party, adding or changing parties, the terms for player chip redemptions and security, the security for the buyer or seller's obligations, or related to any conditions on the Commission's approval.

(Alternatively, there should be a procedure for submitting the modification to the Commission's Executive Director or Chief Counsel who can decide that the modification does not relate to the reasons why the Commission had to approve the transaction and put the matter on the next consent calendar.)

IX. License Maintenance. §12330(b)

Referring to (b), what process would a security interest holder follow to foreclose on their security interest and be able to operate the licensee? For example, the owner sells their business to a buyer for a substantial down payment and a note. If the buyer defaults on the note and the seller wishes to foreclose and resume operating the cardroom business, what steps does the seller have to follow? In particular, what are the licensing steps?

What should happen is that the seller, who has already been licensed as an owner and has been continuously licensed now as a security interest holder, should not have to be relicensed. Their status as a security interest holder and former owner should enable them to resume operating the business without a new licensing process and delays.

This illustrates a broader problem: the absence of a Commission process for amending an existing license. This arises for example when someone who is licensed wishes to place their interest in trust. Even though they are already a licensed owner, they have to file a new application to become licensed as a trustee instead of just amending the designation on the current license from owner to trustee of an owner. Previously, GPAC recommended to the Commission that there be a process to amend an existing owner's license and provided draft language to accomplish that.

X. Processing Timelines. §12332

As noted before, the Commission should consider a shorter timeline for reviewing modifications to a previously approved transaction under section 12326 (i). Many of these modifications can be put on the consent calendar without substantial delay.

Sometimes there are modifications that are "material" under contract law but from a regulatory perspective are not important to the Commission's original review or reason why the contract required pre-approval in the first instance. The modification should be submitted for review and if on review the Commission staff determines the modification is appropriate for the consent calendar, it should be placed on the next agenda.

Conclusion

Regardless of how long a regulation of this type has been under consideration, the Commission should not advance to formal rule-making until these issues are remedied and another draft can be reviewed, without APA time pressures truncating the discussion and the Commission's research on impacts of the proposed regulation. While Commission staff may present changes on or before the December 13 hearing to address some of these issues, with a regulation of this complexity, it takes time to understand the foreseeable consequences of changes in definitions and requirements. That does not mean that staff should not propose improvements on or before December 13, or that the regulation should suffer from the same delay as after the 2018 workshop. But before starting formal rule-making the Commission should provide direction, re-print the language, then survey the industry and Bureau on the impacts.

Thank you for the opportunity to comment on the proposed regulations.

Sincerely,

/s/

David M. Fried

ROBB & ROSS

JOSEPH W. ROBB A PROFESSIONAL CORPORATION

PHILIP A. ROBB
ALAN J. TITUS
ANNE C. SLATER †
JOSEPH W. ROBB **
**(1926 - 2019)

591 REDWOOD HIGHWAY, SUITE 2250
MILL VALLEY, CALIFORNIA 94941
TELEPHONE: (415) 332-3831
FAX: (415) 383-2074

STERLING L. ROSS, JR. *
*RETIRED

†CERTIFIED SPECIALIST IN ESTATE PLANNING, PROBATE AND TRUST LAW, THE STATE BAR OF CALIFORNIA BOARD OF LEGAL SPECIALIZATION

December 2, 2022

California Gambling Control Commission
Attn: Alex Hunter
2399 Gateway Oaks Drive, Suite 220
Sacramento, CA 95833-4231

Re: Approval of Transactions

Dear Mr. Hunter:

I write on behalf of Artichoke Joe's with comments on the draft regulations referenced above.

As a preliminary comment, these regulations attempt to control two very different types of transactions. One type involves transactions in the normal course of business–the various expenses of running a cardroom. The other involves transfers of ownership interests in the business. The first is done by the business entity; the second by the owners of the business entity. The first are actions in the normal course of business; the second are not. Regulation of the first is not required by the Gambling Control Act; regulation of the second is. Because these two types of transactions are so different, they should be regulated separately, and not be lumped together.

§12002. General Definitions

(d) *"Affiliate" has the same meaning as defined in Business and Professions Code section 19805, subdivision (a), and, for purposes of this division includes the following:*

Although this introduction says that the term "affiliate" has the same meaning as in the Business and Professions Code, in fact, the person included as affiliates in paragraphs (d)(1) through (d)(5) are not consistent with the definition in the Business and Professions Code. The definition in the Gambling Control Act is based on *control* of one person over another, such as a corporation and its

subsidiary. The persons covered by the proposed definition in the regulation is based on the *relationship* between the two persons, not on control.

The statute reads, "'Affiliate' means a person who, directly or indirectly through one or more intermediaries, controls, is controlled by, or is under common control with, a specified person." Affiliation is determined by *control*, a word repeated three times in that single-sentence definition. Thus, a corporation and its subsidiary would be considered affiliates because a subsidiary is under the control of its parent.

The element of control is completely lacking in the regulation. Instead, as further discussed below, it substitutes relationship for control, and bases treatment of affiliation on a relationship. In this way, the regulation is completely at odds with and inconsistent with the statute.

The term affiliate is used in regulation 12326 to require certain transactions to be approved by the Commission. The regulations would require transactions to be approved between persons who are not licensed by the Commission or under the control of persons under Commission authority, and thus exceeds the Commission's authority.

The regulatory definition conflicts with the statutory definition in a second way. Both use the phrase "specified person," but they use the phrase differently. The regulation defines "specified person" as the owner category licensee. The statute does not define the phrase but clearly is not limited to the definition in the proposed regulation. The result is a claim in the regulation that the term has the same meaning as the statute when in fact the two have different meanings.

(d)(1) *Any business entity in which a specified person and that specified person's spouse or registered domestic partner, as applicable, control an individual or combined ownership interest of 10 percent or more.*

This paragraph is based on a close personal relationship and not on legal control of one person by the other, and thus conflicts with the statutory definition. First, if the specified person's spouse is not licensed, the spouse is not under the Commission's authority. A licensee might have a close relationship with their spouse, but that is not the same as legal control. One spouse cannot force the other spouse to do something against their will. Second, ownership of 10 percent of a business entity does not necessarily provide control over that entity. If the

licensee does not have control over the business entity, this regulation is beyond the Commission's authority.

(d)(2) *A director, officer, general partner, managing member or person in control of any business in which the specified person and specified person's spouse or registered domestic partner, as applicable, control an individual or combined interest of 10 percent or more.*

This paragraph is based on close personal and business relationships but not on legal control, and thus conflicts with the statutory definition. This paragraph compounds the defects of the prior paragraph. Ownership by the specified person's spouse does not provide the specified person with legal rights to control the business, let alone to control the specific individuals involved. Nor does ownership of just a 10% interest result in control over the business. Even if the specified person had control over the business, the specified person would not have control over the specific individuals identified. Thus, this paragraph exceeds Commission authority.

(d)(3) *A spouse or registered domestic partner of a specified person.*

This paragraph is based on a close personal relationship between two persons and not on legal control of one by the other, and thus conflicts with the statutory definition. A licensee does not have legal control over their spouse or registered domestic partner, and the definition exceeds Commission authority.

(d)(4) *A person who resides in the same home as a specified person and is:*
(A) The father, mother, or sibling of the specified person or the specified person's spouse or registered domestic partner;
(B) The child or grandchild of the specified person; or,
(C) The spouse or registered domestic partner of a child of the specified person.

This paragraph is based on a close personal relationship between individuals but not on legal control of one person by another, and thus conflicts with the statutory definition. The fact that a licensee's parents or siblings or children or grandchildren, or the spouses of the licensee's children reside with a licensee does not endow the licensee with legal control over them. Thus, this paragraph exceeds the Commission's authority.

(d)(5) *Any trust or estate in which a specified person, or a specified person's spouse or registered domestic partner, is a beneficiary, or serves as trustee or trustor of a revocable trust, or in a similar fiduciary capacity.*

There are three problems in the proposed text. First, this paragraph is based on a relationship and not on legal control, and thus conflicts with the statutory definition. A licensee who is a beneficiary of a trust has no legal control over the trustee. As discussed above, a licensee has no legal control over his or her spouse, and if the spouse is just a beneficiary, the spouse has no legal control over the trustee. Where the licensee has no legal control, the regulation exceeds Commission authority. Second, a trustor of a trust is not said to "serve as trustor." That is not correct usage and creates a lack of clarity. A trustor is a person who created or settled the trust over the trust property. Third, the phrase "in a similar fiduciary capacity" is vague. What would be a similar fiduciary capacity? If there is no specific meaning to this, it should be deleted.

§12054. Consideration at a Commission Meeting

(a)(12) *Determine that an unlicensed person requires licensure, or that a licensee requires additional licensure.*

The phrase "*additional licensure*" is not clear. What is "additional licensure?" The Gambling Control Act requires that certain persons be licensed, and requires investigation. The criteria for licensing of an individual in one capacity is the same as for a different capacity. See Bus. & Prof. Code §§19857 and 19859. Once a person is licensed, what more is needed to be determined? This should be clarified.

CHAPTER 5. ACCOUNTING AND TRANSACTION APPROVALS
ARTICLE 1. Definitions and General Provisions

§12311. Definitions

(b)(8) *'Transaction' means any business activity that establishes or modifies any rights, powers, privileges, obligations, duties, or liabilities in which goods, services or monies are exchanged, or any transfer or assignment of an interest through a gift.*

This definition is long, abstract, and unclear and seems to vary widely from the common dictionary definition of the term.

The Oxford American Dictionary ("OAD") defines the word "transaction" as, "An instance of buying or selling something." (p. 1796). Online, Investopedia defines the word "transaction" as "a completed agreement between a buyer and a seller to exchange goods, services, or financial assets in return for money." Those definitions are much clearer than the one proposed.

The law allows legislators and regulators to prescribe legal definitions, but only "within reasonable limitations." *In re Monrovia Evening Post*, 199 Cal. 263. The proposed definition is not within reasonable limitations as it lacks clarity and is not reasonably related to common usage of the term.

There are four operative phrases. The first phrase applies to "any business activity." The second phrase "that establishes or modifies any rights, powers, privileges, obligations, duties, or liabilities" modifies activity. The third phrase "in which goods, services or monies are exchanged" also seems to modify "activity." The fourth phrase includes gifts. I look at each phrase separately below.

The first phrase, "any business activity," is not found in common dictionary definitions and seems intended to exclude personal transactions. If a shareholder of a corporation which operates a cardroom owns the stock as a personal investment and sells the stock, that would seem to be outside this definition.

The second phrase "that establishes or modifies any rights, powers, privileges, obligations, duties or liabilities" modifies activity. This language is not normative in other definitions of "transaction." Further, the concepts are very abstract and it is not clear what types of business activities are covered by each of the six terms. Is this phrase necessary? Does it encompass some business activity that would not be encompassed by just including the third phrase? Even if so, are all six terms necessary?

The third phrase, "in which goods, services or monies are exchanged," is a normative definition. Presumably it modifies the word "activity, but if so, there should be an "and" in front of the phrase to indicate that both the second and third phrases modify the same word.

The fourth phrase, including gifts, is also ambiguous. Is this just referencing transfer of ownership interests in the business entity or does this include some other interests? Further, a gift is not an exchange and thus is not a transaction. It is a transfer between two parties, but not an exchange. Thus including gifts as

"transactions" would be beyond normal usage of the word. We question whether this is necessary given that the regulation requiring approval of transfers of stock would cover transfers resulting from gifts within their inclusion in the definition.

§12311.2. General Provisions

(b) *All writings and supporting documentation required to be maintained by this article must be made available to any law enforcement agency or federal, state, or local regulator.*

This regulation is not consistent with existing Constitutional or statutory law. The Fourth Amendment protects persons from unreasonable search and seizure and requires agencies to obtain search warrants upon a showing of probable cause to a neutral judge. The Bureau, in its regulatory role, has access to some records without a search warrant, but the Commission has no authority to exempt other agencies from Constitutional requirements.

(c) *[]*

Subparagraph (c) is missing, and subparagraphs (d) through (j) should be renumbered.

(d) *A transaction is considered effective on the contract date,...."*

This is unclear, but further, it can be inconsistent with the facts and with other law. A contract date (the date a contract is made) can be different from its effective date. A contract can be made binding on the date of signing, a future date, or a prior date (backdating). Is this regulation saying that even if the parties agree, consistent with contract law, that the contract is not effective until some future date or future event and therefore under law, the contract is not effective, Commission regulation will treat the contract as effective? If so, the regulation would create an inconsistency in law. Further, it is not clear why this rule is necessary.

(g) *Patron chip transactions, extension of credit to patrons, player's banks, and patron check cashing are exempt from this article.*

The proposed language exempts chip transactions from "this article" unchanged from the 2018 draft. However, the regulations have been restructured

into multiple articles. I think the intent is to provide an exemption from all of Chapter 5, not just Article 1 which contains only definitions and general provisions.

§12312. Record Retention and Maintenance

(a) *Notwithstanding Section 12003, all records required by this chapter must be maintained for a minimum of seven years.*

Rather than state an exception to 12003 in this regulation, section 12003 should be amended to state, "Except as provided in section 12312...." That way, people looking at section 12003, which has a shorter retention period, will not be misled.

§12313. Financial Statements and Reporting Requirements

(f) *Maintain fiscal year accounting on a calendar year basis ending December 31 of every year.*

Aside from the fact this is an incomplete sentence, it violates federal and state statutes. Under federal and state tax law, taxpayers are allowed to have a fiscal year end that ends on the last day of any month of the year. *See* Internal Revenue Code 26 USC §441; Calif. Rev. & Tax. Code §17551. By requiring that fiscal year accounting be kept on a calendar year, the regulation would be inconsistent with tax statutes. Further, this is not authorized by the Gambling Control Act and is not necessary.

Article 3. Transaction Requirements

§12322. General Requirements and Conditions

(a) *All transactions requiring prior approval pursuant to this article must contain a provision that the license is subject to the provisions of the Act and the regulations of the Commission and the Bureau.*

This regulation is not clear. Does it mean that documentation of a transaction must contain the required provision? What if the transactions is not documented or the transferee doesn't sign the documentation? For example, if a parent gifts stock to a child, the child usually will not be required to sign any documentation. For another example, section 12326(g) would require Commission

approval of employment of a person who has been denied a license, but employment of a person is often done without any written employment agreement. How does this regulation apply in those situations?

(b) *A transaction to sell or lease real property or an interest in real property when the Commission required the purchaser or lessee to be approved or licensed for a reason associated with the property must contain a provision regarding responsibility for payment of any fees due pursuant to any subsequent deficiency determination made under the Act.*

This regulation fails to follow the language of the statute, and as a result is unclear. We suggest more closely following the language of the statute as follows:

> Pursuant to section 19903, when any person contracts to sell or lease any property or interest in property, real or personal, under circumstances that require the approval or licensing of the purchaser or lessee by the commission pursuant to subdivision (a) of Section 19853, the contract shall contain a provision satisfactory to the commission regarding responsibility for the payment of any fees due pursuant to any subsequent deficiency determinations made under this chapter that shall encompass any period of time before the closing date of the transaction.

(d) *... This provision does not prevent the payment of any taxes, operating expenses, preexisting obligations, preexisting dependent support, payment for debts related to the purchase of any ownership interest in a licensee, or any other distributions of proceeds that is approved by the Commission.*

This phrase "payment for debts" is not parallel to the other phrases, and the phrase "that is approved by the Commission" could modify all the elements in the list or just the last element. We suggest the following changes:

> This provision does not prevent the payment of any taxes, operating expenses, preexisting obligations, or preexisting dependent support, payment ~~for~~ of debts related to the purchase of any ownership interest in a licensee, or payment of any other distributions of proceeds that is approved by the Commission.

(f) *Any document whose purpose is to represent an ownership interest in a licensee must include the legend provided in paragraph (1) in the body of the document or as an attachment to the document.*

It is not clear if this section is requiring that the legend be placed on all currently existing and issued ownership documents or if it applies only to documents issued in the future. That should be clarified. Also, we suggest that the phrase "the legend provided in paragraph (1)" be simplified to read "the following legend:...." That would be followed by the legend in the same subsection.

(g) *All transactions requiring prior approval pursuant to this article cannot specify a closing date, or include any provisions that allows for any party to the transaction to perform any duty or obligation, confer any benefit, or receive any right, benefit, service, privilege, compensation, interest, or assignment of interest prior to the approval of the transaction by the Commission.*

The prohibition against any provision requiring a party to perform "any duty or obligation" is too broad. Transactional agreements will sometimes require one party to apply to the Commission for approval of the transaction or require one party to pay the other's costs of applying. Further, sometimes the contract for purchase of a business will require the seller to keep operating or might prohibit the operator from taking cash out of company. Those type of provisions do not offend licensing principles and should not be prohibited. Also, the prohibition against specifying any closing date is more restrictive than necessary. A contract could specify a closing date a specific number of days after Commission approval, and the regulation should be modified to read, "...cannot specify a closing date prior to Commission approval of the transaction."

§12324. Reporting Requirements

(a) *All transactions conducted by an owner category licensee must be reported annually to the Bureau.*

Who must report

In requiring all "owner category licensees" to submit reports, this would apply not just to the business entity (the "owner licensee") but to all the endorsee licensees. Although the Gambling Control Act defines "owner licensee" to include

only the owner of a gambling enterprise who holds a state gambling license, the regulations define this term differently. Under Reg. 12002(aj), the term "owner category license" includes the "cardroom owner type license" and under Reg. 12002(ai), the term "cardroom owner type license" includes "all cardroom business licenses and all cardroom endorsee licenses."

This creates some uncertainty as the term transaction applies to "business activity" but most of the transactions (using a dictionary definition) that a cardroom endorsee would transact would be personal, buying food and clothes, paying utilities, rent or a mortgage. We oppose requiring endorsee licensees to file transaction reports of business transactions, let alone of personal transactions.

Which Transactions to Report

The requirement to report all transactions would expand on current practices and would create a waste of time and expense on both sides.

Currently, and for a number of years, as part of the renewal of a cardroom license, the Bureau requests a list of contracts and agreements. The focus is on the contract. All amounts paid to the particular vendor can be lumped together in one entry. These new regulations would change the focus from the *contract* to each *transaction* under the contract, and require itemization of each transaction. For those cardrooms which have significant food operations, a single vendor can deliver a few times a week, and these regulations will increase the workload exponentially. A single line entry could now become 100 lines. Requiring this level of detail is not necessary. If the Bureau needs to see more detail, the Bureau can request detail or even undertake an audit of the records.

Also, currently the request is for a list and the cardroom is able to provide an Excel spreadsheet. However, the proposed regulation requests a "summary" and seems to require a narrative on each individual transaction rather than a list. A list is far easier to assemble than a narrative summary, and given that a list is all that has been required for many years, that should be adequate.

The regulation should contain a minimum threshold, below which reporting is not required. For example, if a vendor supplied services on a one-time basis for $1,000, the cost of reporting and reviewing simply is not justified. We suggest a minimum threshold of $25,000.

Last, reporting on engagement of lawyers for legal representation would infringe on the attorney-client privilege and is not justified. An exception should be made for engagement of attorneys for legal services.

§12326. Commission Approval of Transactions

Intro *Licensees must submit the following transactions to the Bureau for review and must receive approval from the Commission before any party to the transaction performs his, her, or its duties or obligations, confers any benefit, or receives any right, power, benefit, service, privilege, compensation, interest, or asignment of interest.*

As with section 12232(g), discussed above, the prohibition against any provision requiring a party to perform "any duty or obligation" is too broad. Transactional agreements will sometimes require one party to apply to the Commission for approval of the transaction or require one party to pay the other's costs of applying. Further, sometimes the contract for purchase of a business will require the seller to keep operating or might prohibit the operator from taking cash out of company. Those type of provisions do not offend licensing principles and should not be prohibited.

(b) *The sale, assignment, transfer, pledge, or other disposition of an option to purchase any ownership interest in a licensee.*

This language is unclear. This seems to apply to a transfer of an option but not to the creation or issuance of the option in the first place. If that is correct, why does it apply to one and not the other? Options allow a holder to exercise a right to buy (or to sell), but do not result in a purchase or sell unless the option is exercised. Usually some time after exercise of the option, the purchase or sale will close. Given that neither issuance, creation or transfer of an option change ownership of the interest or affect the rights of an owner of the interest or creates any rights in the optionee, there is no need for approval of the Commission to any of these transactions. Once the option is exercised, it is akin to entering a purchase and sale agreement, and at that point, Commission approval should be required. Before that, reporting of the issuance of the option or its transfer should be sufficient.

In this regard, sometimes an option could be issued based on conditions that never come to fruition. For example, A could provide B an option to purchase A's

stock if B survives A. However, if B does not survive, the option expires. Any prior approvals would have been a waste of time and effort.

As a possible exception, there may be reason to require Commission approval in a couple unusual situations. Sometimes, an optionee will pay for the option. This is akin to issuance of a security, and in those rare situations, it would make sense to require prior approval. Presumably, before a buyer paid for an option, the buyer would want to know he or she could obtain a license. Second, sometimes, options are issued in lieu of other compensation. Here too, it would make sense to require prior approval.

(c) *The transfer of possession, ownership, or title of a security interest provided for in subdivision (a) of Business and Professions Code section 19900.*

Section 19900 prohibits *enforcement* of a security interest without prior approval of the Commission. However, the statute does not require prior approval of either initial grant of the security interest or its subsequent *transfer*. This makes sense. There is good reason to require prior approval of *enforcement* of the security interest. In that situation, the prior holder of a security interest converts the security into an ownership interest. That same reasoning does not apply, however, when the security interest is first granted or if the security interest is transferred, and in those cases, there is no reason for requiring Commission approval.

(d) *The sale, lease, interest, transfer, assignment, encumbrance, or other disposition of any real property associated with a licensee when the Commission has previously required the owner of that real property to be licensed or approved for a reason associated with the property.*

The word "interest" in the first line does not make sense. The other nouns are verbal nouns describing an activity. Interest is not a verbal noun. Perhaps this was intended to read, "The sale, lease, transfer, assignment, encumbrance, or other disposition of any *interest* in any real property...."

(e) *...This provision does not apply to an institutional investor.*

The word "investor" should be "lender." It should read "institutional lender."

(f) *Any transaction agreement between a licensee, or an affiliate of a licensee, and a person...who has been denied a license by the Commission...*

Should this read "transaction or agreement"? Transaction is a noun, not an adjective, and the phrase does not make sense.

As discussed above, the word "affiliate" is defined to include people not under the control of the licensee, and therefore, this regulation is beyond the authority of the Commission.

(g) *Employment by a licensee or affiliate of a licensee of any person who has been denied a license by the Commission....*

First, as discussed above, the word "affiliate" is defined to include people not under the control of the licensee, and therefore, this regulation is beyond the authority of the Commission. Second, this regulation does not really have to do with transactions. It has to do with employment and is out of place.

(h) *The creation of any trust or estate that permits a person to take part in the operation of a licensee, or that provides payment to a person, bypass trust, or subtrust from the profits of a licensee.*

This regulation presents a number of problems. First, the creation of a trust is not a transaction. Second, the phrase "permits a person to take part in the operation of a licensee" is unclear. How would a trust or estate permit a person to take part in the operation of a licensee unless the trust was a shareholder? Third, trusts do not provide for "payments." Rather trusts provide for distribution of income and principal. Fourth, similar to the second point, how would the trust hold "profits of a licensee." That would be the case only if the business were a sole proprietorship. If the assets are held in some sort of business entity, the trust will be an endorsee license. Distribution from a business entity to its owners is allowed without commission approval, and so should this. Fifth, we do not understand the singling out of bypass trusts. Sixth, the distributions from a trust would not be "from the profits of a licensee." The distribution from the entity might be from the profits of the licensee but in the hands of the trustee, the money is either income or principal, and distribution from the trust is of income or principal.

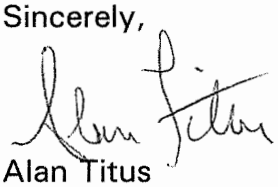
§12328. Transactions and License Requirements

The Transaction Review Request Form, section 3, uses the term "Institutional Investor," and as discussed above, I think the correct term is "institutional lender."

*

We appreciate your consideration of these comments.

Sincerely,



Alan Titus

ROB BONTA
Attorney General

State of California
DEPARTMENT OF JUSTICE

BUREAU OF GAMBLING CONTROL
P.O. BOX 168024
SACRAMENTO, CA 95816

December 2, 2022

Alex Hunter, Legislative and Regulatory Specialist
California Gambling Control Commission
2399 Gateway Oaks Drive, Suite 220
Sacramento, CA 95833

RE: Approval of Transactions - CGCC-GCA-2022-0X-R

Dear Alex Hunter:

The Department of Justice, Bureau of Gambling Control (Bureau) has reviewed the California Gambling Control Commission's (Commission) draft regulations, which were routed on November 9, 2022, concerning Approval of Transactions. We respectfully submit the following comments for consideration. Proposed modifications to the regulatory text are indicated with an underline or by strikeout.

California Code of Regulations, title 4, section 12002. General Definitions.

Subject: Subdivision (d)(5)(ao) – Definition of Specified Person

The proposed definition of "Specified Person" states that an owner category licensee who is a natural person, unless the natural person controls less than a 10 percent ownership interest *and would not otherwise require licensure*. Business and Professions Code, section 19852 requires all owner category licensees to be licensed. The intent of this section is unclear.

California Code of Regulations, title 4, section 12311.2. General Provisions.

Subject: Section 12311.2 – Subdivision Numbering

Proposed section 12311.2 appears to have misnumbered subdivisions (d) through (j) because it is missing subdivision (c).

Subject: Subdivision (b)(1) – Requests to Inspect, Copy, or Audit Documents

Proposed section 12311.2, subdivision (b)(1) imposes a requirement upon the Bureau that is inconsistent with the Gambling Control Act. Business and Professions Code section 19827 provides that the Bureau, upon approval of the chief, and without notice or warrant, has the authority to demand access to, and inspect, examine, photocopy, and audit all papers, books, and records of an owner licensee on the gambling premises in the presence of the licensee or his or her agent. (Bus. & Prof. Code, § 19827, subd. (a)(1)(E).) Proposed section 12311.2, subdivision (b)(1) thus imposes restrictions upon the Bureau's statutory authority to access, inspect, copy, or audit any licensee

records, upon demand, by requiring a 10 business day request period, and by requiring that the request be made in writing. The Bureau recommends deleting subdivision (b)(1) of proposed section 12311.2 as it is contrary to Business and Professions Code section 19827.

Subject: Subdivision (b)(2), (2)(A), (2)(B) – Requests for Documents by Other Law Enforcement Agency or Federal, State, or Local Regulator

Proposed section 12311.2, subdivision (b)(2), and its subparts, impose requirements upon the Bureau and other law enforcement or regulatory authorities prior to requesting, and obtaining, writings and documentation required to be maintained by licensees. These requirements may be inconsistent with the document inspection authorities of the various state, federal, or local law enforcement agencies, and regulators.

The requirement that a request for documents by a law enforcement or regulatory agency be related to a "specific topic or area" is incompatible with certain law enforcement or regulatory investigative matters, and could compromise an ongoing investigation. To require that a law enforcement or regulatory agency specify topics or areas of inquiry may be contrary to the laws underlying that law enforcement or regulatory authority. This proposed subdivision also appears to impose requirements or conditions upon agencies outside the scope of the Commission's authority to regulate. If a licensee is required by law (or a court order) to provide documents to a law enforcement or regulatory agency, without conditions or under different conditions or circumstances, the requirements imposed by this proposed subdivision would be in conflict with those laws.

In addition, the requirement that the Bureau have previously communicated to the licensee that the Bureau is working with another law enforcement or regulatory agency in order for a request to be valid is problematic for at least the following reasons:

1. The Bureau may not be aware of a particular law enforcement or regulatory activity that another law enforcement or regulatory agency may be conducting, and thus cannot provide a licensee with the communication or notification that is proposed to be required;
2. Even if the Bureau were aware of certain law enforcement or regulatory activity, the Bureau may not be "working in conjunction with the Bureau" on the "specific topic or area"; and,
3. Even if the Bureau were aware of certain law enforcement or regulatory activities, the disclosure of those activities, the Bureau's involvement therewith, or the "specific topic or area" of those activities may either (a) jeopardize the integrity of an investigation or other regulatory activity, or (b) may violate the Bureau's obligation to maintain the confidentiality of those investigative or regulatory activities.

The Bureau recommends deleting subdivision (b)(2), and its subparts, of proposed section 12311.2.

Subject: Subdivision (d) – Transaction Effective Date

Proposed subdivision (d) which specifies the "effective date" of a particular transaction may interfere with a licensee's ability to consummate a transaction, depending on the terms and conditions appurtenant thereto. The "effective date" of a transaction is a matter typically negotiated between the parties to a transaction, and has implications on other obligations that the parties to the

contract are required to undertake. Additionally, this subdivision would require the Bureau to determine "when," precisely, a contract has been formed for purposes of determining the "contract date." The proposed terms of a contract may be altered or go through different versions or iterations, and it would be difficult for the Bureau to determine, on that basis, what the "contract date" would be.[1] The most reliable date upon which the Bureau may determine the effective date would be through the terms of a transaction itself, as determined by the parties to the transaction. The Bureau recommends that this subdivision be deleted.

Subject: Subdivision (f) – Transactions Conducted with an Institutional Investor

While institutional investors may be exempt from the licensure requirements under the Gambling Control Act, the Bureau would only be made aware of a transaction affecting the ownership interests in a gambling enterprise, if ever, through an annual licensing review, unless notified in advance by a licensee. The Bureau recommends requiring that a licensee provide the Bureau with a notification of the proposed transaction with a purported institutional investor, with sufficient information for the Bureau to ascertain whether the purported institutional investor falls within the definition specified in the Gambling Control Act, and that no licensure is required.

California Code of Regulations, title 4, section 12313. Financial Statements and Reporting Requirements.

Subject: Subdivision (f) – Fiscal Year Accounting

As drafted, proposed subdivision (f) requires a business entity to maintain a fiscal year accounting on a calendar year basis ending December 31 of every year. The Bureau recommends deleting this subdivision as a gambling enterprise should have the ability to make decisions concerning general business practices.

California Code of Regulations, title 4, section 12322. General Requirements and Conditions

Subject: Subdivision (a) – Licensee Subject to the Provisions of the Gambling Control Act, and Regulations of the Commission and the Bureau

Proposed section 12322, subdivision (a) imposes a condition that transactions that require the prior approval of the Commission under Article 3 contain a provision that the licensee is subject to the Gambling Control Act, and the regulations of the Commission and the Bureau. This requirement appears redundant. Licensees are by definition required to abide by the Gambling Control Act and the regulations promulgated thereunder. It appears instead that the aim of this subdivision is to require that the terms of the transaction state that the transaction is subject to the Gambling Control Act and the regulations, and that approval of the transaction is required to comply with those laws. The Bureau recommends that this subdivision be clarified to state that requirement, if that is what is intended.

[1] For example, if two parties agree to the sale of an interest in a gambling enterprise (e.g., "I agree to purchase your shares in a gambling enterprise for a specified amount of money"), without further and final terms being established, it could be argued that the "contract date" is the date upon which that agreement to sell/purchase was made.

Subject: Subdivision (g) – Receipt of Approval by the Commission Prior to the Performance of Any Duties or Obligations

Proposed section 12322, subdivision (g) provides, among other things, that a transaction cannot include any provision that allows a party to the transaction to perform any duty or obligation prior to approval of the transaction by the Commission. This subdivision would prohibit a transaction from including a closing date. The Bureau notes that many of the transactions that it reviews include a closing date that is specified as occurring after the parties to the transaction obtain Commission approval. Additionally, without a date specified in the transaction, the parties would not be able to determine when actual transfer of any interests will occur. The Bureau recommends amending subdivision (g) to require a closing date that occurs after the Commission has approved the transaction.

Additionally, this subdivision would prohibit the performance of many acts which are condition precedent to the performance of other duties and obligations necessary to consummate a transaction.[2] This may result in transactions being voided or abandoned by a party to the transaction,[3] resulting in wasted Bureau and Commission time and resources. The Bureau recommends instead that subdivision (g) be amended to instead require a transaction to include restrictions on an unlicensed party to a transaction from taking any action, or obtaining or exercising any authority for which a state gambling license is required prior to obtaining a license.

The Bureau recommends the following amendments in accordance with the comments above:

(g)(1) All transactions requiring prior approval pursuant to this article ~~cannot~~must specify a closing date, if at all, that occurs after the Commission approves the transaction~~,~~.
(2) ~~or include any~~All transactions requiring prior approval pursuant to this article must include a provision that ~~allows for~~prohibits any unlicensed party to the transaction ~~to~~from performing any duty or obligation, receiving or conferring any benefit, or receive~~e~~ing any right, benefit, service, privilege, compensation, interest, or assignment of interest prior to ~~the approval of the transaction by the Commission~~obtaining the required license.

California Code of Regulations, title 4, section 12326. Commission Approval of Transactions.

Subject: Section 12326 – Commission Approval of Transactions

The first paragraph of proposed section 12326 is unclear, and appears to be duplicative of proposed section 12322, subdivision (g). The Bureau recommends clarifying the intended meaning of the first paragraph of proposed section 12326.

[2] E.g., the payment of deposits, financial assessments and other due diligence activities, obtaining other consents and approvals, such as local government licensing or permitting requirements.
[3] If, for example, a due diligence examination by a buyer determines that there are valid reasons under the contract terms to cancel or void the contract, which would necessarily, under this subdivision, not occur until after the Bureau and Commission have expended the time necessary to approve the transaction.

Subject: Subdivision (h) – Creation of a Trust or Estate

Proposed subdivision (h) is underinclusive, because it omits the amendment of a trust or estate that permits a person to take part in the operation of a licensee, or which provides payment to a person, bypass trust, or subtrust from the profits of a licensee. The Bureau recommends the following amendments:

> (h) The creation or amendment of any trust or estate that permits a person to take part in the operation of a licensee, or that provides payment to a person, bypass trust, or subtrust from the profits of a licensee; and/or,

California Code of Regulations, title 4, section 12328. Transactions and License Requirements.

Subject: Subdivision (a) – Transaction Review Request Form [CGCC-CH5-XX]

The Bureau proposes to update its contact information on page 1. This proposal will ensure that applicants and licensees have a means to contact the Bureau during the transaction review process.

MAIL COMPLETED FORM AND DEPOSIT TO:
BUREAU OF GAMBLING CONTROL
P.O. Box 168024
Sacramento, CA 95816-8024
~~(916) 227-3584~~(916) 830-1700

California Code of Regulations, title 4, section 12330. Required License Maintenance.

Subject: Subdivision (b) – Security Interest Holder

The proposed text in subdivision (b) of section 12330 states the seller or transferor may hold a valid license as a "security interest holder" if they maintain a security interest in the licensee. It is unclear whether the definition of "security interest" holder is consistent with the definition provided under Chapter 5. Accounting and Transaction Approvals, section 12311, subdivision (b)(7). The Bureau recommends amending language in subdivision (b) to clarify that a seller or transferor are required to be licensed as a financial interest holder.

> (b) If the seller or transferor maintains a security interest in the licensee, the seller or transferor may choose to maintain a valid license as a ~~security~~financial interest holder endorsed on the purchaser's or transferee's license, if not otherwise required by the Commission.

California Code of Regulations, title 4, section 12332. Processing Timelines for Transaction Requests.

Subject: Subdivision (a) – Transaction Request Submittal

The Bureau requests the following amendment to specify a request for the review of a transaction must be submitted to Bureau:

(a) A request for the review of a transaction must be submitted to the Bureau and processed within the following timeframes:
…

Subject: Subdivision (a)(3) – Processing Timelines for Transaction Requests

Proposed subdivision (a)(3) appears to conflict with Business and Professions Code section 19868. The Bureau requests the following amendment to the proposed language:

(3) Within 90 calendar days of receiving a complete request or ~~within 180 calendar days of receiving a request~~ if the request is accompanied by a license application, within the timeframe specified in Business and Professions Code section 19868, the Bureau must submit the transaction to the Commission for consideration, including any appropriate recommendation related to the transaction and stating whether any licensure, registration, or a finding of suitability may be necessary. Upon the submission of a transaction to the Commission, the Bureau must send a copy of any recommendations it provided to the Commission, to the licensee.

Thank you for considering our comments. Please contact Andreia McMillen at Andreia.McMillen@doj.ca.gov if you have any questions.

Sincerely,

YOLANDA MORROW
Director

For ROB BONTA
Attorney General