

STATE OF MINNESOTA
DEPARTMENT OF PUBLIC SAFETY
GAMBLING ENFORCEMENT DIVISION

**In The Matter Of The Proposed Rules Of
The Department Of Public Safety Governing
The Licensing Of Manufacturers And
Distributors of Gambling Devices**

**STATEMENT OF
NEED AND
REASONABLENESS**

General Statement

The Gambling Enforcement Division was created in 1989 by an act of the Minnesota Legislature. The Gambling Enforcement Division is a division of the Department of Public Safety. The division is tasked with providing investigative and enforcement services to the Minnesota State Lottery, the Minnesota Racing Commission, the Gambling Control Board. The division is also involved in investigation and enforcement related to Indian gambling and unlawful gambling activities. The types of investigations conducted by the division include criminal investigations, licensing investigations, annual lottery security audits, and gambling employee background investigations.

In 1991, the Legislature established a licensing requirement for manufacturers and distributors of gambling devices. The responsibility for this function was given to the division.

The division, in assessing the legislation, determined that rules would be needed in order to effectively administer the licensing process. In creating rules, the division looked to other jurisdictions performing similar functions. Those jurisdictions included South Dakota, Montana, Nevada, and New Jersey, as well as existing Minnesota statutes and rules. The proposed rules reflect what is used by other jurisdictions in the licensing and regulation of the gambling industry.

Statutory Authority

Minnesota Statutes, section 299L.07 (as enacted by Minnesota Laws 1991, chapter 336, article 2, section 9), requires a person to obtain a license from the Commissioner of Public Safety before manufacturing or distributing gambling devices. This law is effective January 1, 1992. These rules set out the requirements for licensing and for licensees.

The Commissioner's authority to adopt rules comes from Minnesota Statutes, section 299L.03, subdivision 8, which states: "The commissioner may adopt rules, including emergency rules, under chapter 14 to carry out the commissioner's duties under this chapter." The Commissioner also has general rulemaking authority under Minnesota Statutes, section 299A.01, subdivision 6, "to promulgate such rules pursuant to chapter 14, as are necessary to carry out the [duties of the Commissioner]."

Small Business Considerations

Minnesota Statutes, section 14.115, requires the Department of Public Safety to consider the effect on small businesses when it adopts rules. The rules will have a direct effect on small businesses engaged in the manufacture and distribution of gambling devices. Based on the applications for licensure filed with the Division, the number of businesses affected by the rules will be less than 50, of which about one-third are located outside of Minnesota. Most of these businesses are small businesses.

Section 14.115, subdivision 2, states in part:

"When an agency proposes a new rule, or an amendment to an existing rule, which may affect small businesses . . . , the agency shall consider each of the following methods for reducing the impact of the rule on small businesses:

(a) the establishment of less stringent compliance or reporting requirements for small businesses;

(b) the establishment of less stringent schedules or deadlines for compliance or reporting requirements for small businesses;

(c) the consolidation or simplification of compliance or reporting requirements for small businesses;

(d) the establishment of performance standards for small businesses to replace design or operational standards required in the rule; and

(e) the exemption of small businesses from any or all requirements of the rule."

The legislature, in enacting the enabling legislation, placed controls over a previously unregulated industry in Minnesota. For this reason, any rules will have more of an impact than was previously experienced by this industry. The Department has, however, considered specific methods for minimizing the impact of the rules on small businesses. The impact of the rules on small businesses has been minimized as follows:

- a. Less stringent requirements. A great deal of information is required to be included in the application for licensure. It should be noted that gambling is a heavily regulated industry wherever it exists in the United States. It should also be noted that in many states, the application for a gambling license is much more involved than the application information required under these rules. Further, we have worked to ensure that the required information on shipment of devices is consistent with that required by other jurisdictions, including the federal government.
- b. Less stringent schedules. Reporting of devices stored in Minnesota is required to be made on a quarterly basis under part 7570.0030. Quarterly reporting was used instead of on a more frequent basis as a consideration for the businesses that are licensed under the rules. Further, quarterly reporting is consistent with other types of business reporting, such as tax reporting.
- c. Consolidation or simplification of requirements. The information to be reported on shipments of gambling devices is consistent with the information to be reported to the United States Department of Justice.

- d. Performance standards. The standards established by these rules are reporting standards, not design or operational standards.
- e. Exemption. The only exemption related to the rules is created by statute to allow an individual to sell one machine annually for personal use. See Minnesota Statutes, section 299L.07, subdivision 1, clause 5. Any further exemption that would apply to small businesses would not be appropriate because it would be contrary to the statutory objective of monitoring and regulating gambling devices stored in and shipped to Minnesota.

Fees Imposed By The Rules

These rules, in part 7570.0020, subpart 6, set an investigation fee to cover the costs of the investigation authorized by Minnesota Statutes, section 299L.07, subdivision 5. This fee is designed so that it covers the actual direct costs of the investigation. Minnesota Statutes, section 16A.128, subdivision 2, states that this fee need not be fixed by rule since it covers the actual direct costs of a service. Since this fee does not have to be fixed by rule, the approval of the Commissioner of Finance is not required under section 16A.128, subdivision 1a, and the Department is not required to send a copy of the Notice of Intent to Adopt and the proposed Rules to the chairs of the House Appropriations and the Senate Finance Committees under section 16A.128, subdivision 2a.

Other Statutory Requirements

Minnesota Statutes, section 14.11, subdivision 1, does not apply because adoption of these rules will not result in additional spending by local public bodies in excess of \$100,000 per year for the first two years following adoption of the rules. Minnesota Statutes, section 14.11, subdivision 2, does not apply because adoption of these rules will not have an impact on agricultural land. Minnesota Statutes, sections 115.43, subdivision 1, 116.07, subdivision 6, and 144A.29, subdivision 4, do not apply to these rules.

Witnesses

If these rules go to a public hearing, the witnesses listed below may testify on behalf of the Department in support of the need for and reasonableness of the rules. The witnesses will be available to answer questions about the development and content of the rules.

- John Willems, Special Agent for the Gambling Enforcement Division, will testify to the intent of the rules and the enabling legislation and to the development of the rules.
- John Garry, Special Assistant Attorney General, will testify to the statutory authority of the rules and the procedures for license withdrawal.
- Tom Brownell, Director of the Gambling Enforcement Division, will testify regarding the need for the rules as well as the function of the Gambling Enforcement Division.
- Any other employee of the Gambling Enforcement Division or the Minnesota Department of Public Safety.

Rule-By-Rule Analysis

7570.0010 DEFINITIONS.

Subpart 1. **Scope.** This subpart sets out the scope of the definitions as applying to this chapter of the rules.

Subpart 2. **Commissioner.** This subpart defines the term "commissioner". This definition comes from Minnesota Statutes, section 299L.01, subdivision 1, but includes a reference to an authorized agent to make clear that the commissioner can act in a personal capacity or through persons authorized to act for the commissioner.

Subpart 3. **Director.** This subpart defines the term "director". This definition comes from Minnesota Statutes, section 299L.01, subdivision 1, but includes a reference to an authorized agent to make clear that the director can act in a personal capacity or through persons authorized to act for the director.

Subpart 4. **Distributor.** This subpart adopts the definition of "distributor" from Minnesota Statutes, section 299L.01, subdivision 1, paragraph (f).

Subpart 5. **Manufacturer.** This subpart adopts the definition of "manufacturer" from Minnesota Statutes, section 299L.01, subdivision 1, paragraph (e).

Subpart 6. **New gambling device.** The enabling legislation and the rules refer to new and used gambling devices in terms of setting out licensing categories. The term "new gambling device" is defined here because it is not defined elsewhere. This definition is reasonable because it is consistent with the statutory definition of "used gambling device."

Subpart 7. **Used gambling device.** The enabling legislation and the rules refer to new and used gambling devices in terms of setting out licensing categories. The term "used gambling device" is not set out in the definitions section of the enabling legislation, but instead is set out in subdivision 6 of section 299L.07. This definition is repeated here for the convenience of the reader.

7570.0020 LICENSE APPLICATION, ISSUANCE, AND RENEWAL.

Subpart 1. **Contents of application.** The items of subpart 1 list the information that must be in an application for a license to manufacture or distribute gambling devices. In general, this information is necessary to identify an applicant and to determine if the applicant is eligible to receive a license. The need for and reasonableness of each item is discussed separately below.

It should be noted that the information required for this license is considerably more in depth than the information required for many other occupational licenses issued by the state of Minnesota. Gambling has the potential for enormous profits if it is run unfairly or illegally. Historically, a criminal element has been attracted to the gambling business because of these potential profits. For this reason, the gambling industry has traditionally been heavily regulated. This heavy degree of regulation is evident in the enabling legislation for this license.

A. This item requires that the application contain the name and all business addresses and telephone numbers. The applicant's name will be used to identify the applicant

and to issue the license in the applicant's name. The addresses and telephone numbers will be used to contact the applicant.

- B. Licenses may only be issued to persons fit to hold a license. It is therefore necessary for the commissioner to investigate the fitness of an applicant before issuing a license. The fitness of an applicant is directly related to the fitness of the individuals and entities that own or control the applicant. This item requires that controlling persons be listed on the application, namely an individual if the applicant is an individual, the partners if the applicant is a partnership, and the directors, officers, and shareholders if the applicant is a corporation. For a publicly traded corporation, shareholders holding less than a 5% interest in the corporation do not need to be listed because, as a practical matter, a such a shareholder has very little control of the corporation and there could be a very large number of this type of shareholder.
- C. This item requires the name, date of birth, social security number, and telephone number of every person listed in item B. This information will be used to conduct the investigation of the applicant. This information uniquely identifies these persons and is easily given by the applicant.
- D. Minnesota Statutes, section 299L.07, subdivision 4, requires that the application contain the names and addresses of any holding corporation, subsidiary, or affiliate of the applicant. This requirement is repeated in the rules so that all application requirements are contained in the rules.
- E. Item E requires that the application contain a history of gambling licensure for the applicant and for every person listed on the application. It is reasonable to ask for this information because it tells how the applicant operates in a gambling environment. This information is commonly required on gambling license applications for other jurisdictions.
- F. Item F asks for the criminal history of the applicant and for every person listed on the application. Minnesota Statutes, section 299L.07, subdivision 3, prohibits the issuance of a license if the applicant or a controlling person of the applicant has been convicted of certain crimes or been involved in illegal business. It is necessary and reasonable to ask for the criminal history so that the commissioner can comply with the statutes in issuing licenses.
- G. The information required by item G relates to the character and integrity of the applicant. To issue a license, the commissioner must determine "that the applicant will conduct the business in a manner that will not adversely affect the public health, welfare, and safety or be detrimental to the effective regulation and control of gambling." Character information relates directly to the determination the commissioner must make in order to issue a license.
- H. Item H requires employment and residence history for persons listed on the application. This information will be used in the commissioner's investigation of the applicant in order to verify that the information contained on the application is true. Employment information shows whether a person has been connected with or engaged in an illegal business. (See, Minnesota Statutes, section 299L.07, subdivision 3, clause (3).) The residence information shows where to look to verify criminal history information.

- I. The application must indicate the class of license sought so that the commissioner can determine if the applicant has submitted the appropriate license fee and so the commissioner can issue the desired class of license.
- J-N. Items J to N require information related to the operation of the applicant's business. Items J and K require financial information. Item L requires information on employees of the applicant. Item M requires information on persons who might share in the profits of the applicant's business. Item N requires the names of persons who have an option to purchase a share of the applicant's business. All of this information is relevant to the ownership and control of the applicant's business. The commissioner will use this information to find persons with direct or indirect financial or management interests in the applicant's business and to verify the information given by the applicant about ownership and control of the applicant's business.
- O. Minnesota Statutes, section 299L.07, subdivision 6, requires the payment of an annual license fee. This requirement is referenced in the rules so that all application requirements are contained in the rules.
- P. Item P requires that the application be accompanied by an authorization for release of information from persons and entities who control the applicant. This requirement serves at least two purposes. One, it puts all controlling persons on notice of the fact that they will be investigated to determine their fitness to hold a license. Two, the authorizations facilitate and reduce the costs of the investigation by eliminating the need for subpoenas.
- Q. Item Q repeats the requirement of Minnesota Statutes, section 299L.07, subdivision 4, clause (3), so that all application requirements are contained in the rules.
- R. This item requires a report on all gambling devices kept under the control of the applicant in Minnesota. This report will be used to verify that the applicant is complying with laws governing the possession and use of gambling devices.
- S. Minnesota Statutes, section 270.72, prohibits the issuance or renewal of a license for the conduct of a profession, occupation, trade, or business if the commissioner of revenue notifies the licensing authority that the applicant owes delinquent state taxes. To administer this statute, the commissioner of revenue requires license applicants to complete a tax information form. This requirement is referenced in the rules so that all application requirements are contained in the rules.
- T. Item T requires that the application be signed by each controlling person, verifying that the information on the application is true. Item T also requires that the signatures be notarized. This requirement helps ensure the accuracy and truthfulness of the information contained on the application.

Subpart 2. **Submission of application.** This subpart requires that an application be submitted to the Gambling Enforcement Division of the Department of Public Safety. This is reasonable because the Gambling Enforcement Division will administer the licensing under these rules for the Department of Public Safety.

Subpart 2 also states that an application is not complete until it meets all the requirements of subpart 1. This makes clear that the commissioner does not have to investigate an applicant or determine whether to issue a license based upon an incomplete application.

Subpart 3. Investigation of applicant's information. Subpart 3 requires the director to investigate the applicant, including its financial and business records. The director has the authority to investigate under Minnesota Statutes, section 299L.07, subdivision 5. Requiring the director to investigate will ensure that accuracy and truthfulness of an application is verified before a license is issued.

Subpart 3 also requires the applicant to make its records and business premises available to the commissioner for inspection. The cooperation of the applicant is absolutely essential to verifying that the information supplied by the applicant is accurate and truthful.

Subpart 4. Issuing or denying a license; basis for determination. Under subpart 4, the commissioner must issue a license if the commissioner determines that the applicant will conduct the business in a manner that will not adversely affect the public health, welfare, and safety or be detrimental to the effective regulation and control of gambling. This criteria comes directly from Minnesota Statutes, section 299L.07, subdivision 3. Items A to I list factors for the commissioner to consider in making the licensing determination. These factors are directly related to the statutory criteria quoted above. It is reasonable to list factors for the commissioner to consider so that the commissioner is consistent in issuing and denying licenses and so that applicants know the basis for issuance and denial.

Subpart 5. Licensing year; partial refund of fee if initial license issued after June 30. The enabling legislation, Minnesota Statutes, section 299L.07, subdivision 6, states, "A license issued under this section is valid for one year." The enabling legislation does not, however, set out the beginning and end of the licensing year. For two reasons, it is important to set out a specific licensing year, instead of having the licensing year be unique to each licensee based on the date the license was issued. One, it eases the burden of administration for the state if all license renewals come due at the same time. Two, the license fees for the different classes of license are based on the number of devices manufactured or distributed in a year. It would be very difficult to enforce or administer the licensing fees requirements if the fees were based on a floating twelve-month period instead of a twelve-month period with a specific beginning and end. Under subpart 5, the calendar year was chosen as the licensing year.

Subpart 5 provides for a refund of one-half of the annual license if an initial license is issued after June 30 of the year for which application was made. An initial licensee is licensed for only the remainder of the year in which the license is issued. The initial licensee does not get the full value of the license fee. Subpart 5 provides a reasonable means of prorating the annual license fee for an initial license. The proration in subpart 5 is similar to that in the statutes that govern the licensing of motor vehicle dealers, which reduce the initial license fee by one-half if the dealer applies after the first half of the licensing year. See, Minnesota Statutes, section 168.27, subdivision 11.

Subpart 6. Investigation fee. The investigation fee is designed to cover the cost of the investigation, which would include expenses for travel, lodging, and incidentals. The fee is required to be deposited in advance to protect the state's financial interest, because the cost of the investigation will be incurred regardless of whether a license is issued. The initial deposits for the investigation fee are set at \$1,500 for in-state businesses and \$5,000 for out-of-state businesses. The difference is based on the increased travel and lodging expenses when traveling out of state. The deposits are based on an estimate of the investigation costs and are intended to be sufficient to initiate the investigation. The fee is reasonable because it is tied directly to the investigation cost; overages are to be refunded and additional funds are to be collected as needed.

Subpart 7. **License classes.** Subpart 7 sets out the license classes created under Minnesota Statutes, section 299L.07, subdivision 6, which assesses annual license fees for the different license classes.

Subpart 8. **Appropriate class of license required.** The enabling legislation created license classes, but did not specify what will happen if a licensee conducts business across a license class. This would occur when a manufacturer or distributor licensed for 100 or fewer devices expands the business to more than 100 devices. This would also occur when a distributor of used devices begins to distribute new devices. This would also occur when a manufacturer begins to distribute devices and vice versa. In each of the above instances, subpart 8 requires a licensee to obtain the appropriate class of license prior to conducting business in the new license class. Subpart 8 also provides for the crediting of fees paid when the additional license covers the activities of the previous license; namely, when a business increases from less than 100 devices to more than 100 devices and when a distributor of used devices begins to distribute new, or new and used devices. Subpart 8 does not credit fees paid when a manufacturer wants to obtain a distributor license or vice versa, but does state that only one investigation fee is required. Subpart 8 is reasonable because it clarifies the statutory licensing categories in a way that allows for the consistent application of these categories.

Subpart 9. **Notice of change.** Subpart 9 sets out the requirements to be used when a change occurs in the ownership or control of the licensee. The department must be kept advised of these changes in order to ensure all persons involved with a licensee meet the requirements established by the legislature and by these rules. The licensee is the party first aware of these changes and is therefore made responsible for notifying the department.

7570.0030 RECORDS REQUIREMENTS.

Subpart 1. **Records kept on devices manufactured, sold, or distributed in Minnesota.** Minnesota Statutes, section 299L.07, subdivision 9, requires a licensee to provide information required by the commissioner relating to the shipment and sale of gambling devices. This subpart refers to the records generated under subparts 2 and 3 and the records required by subpart 4 and requires that these records be kept for three years after the device is disposed of. The three year period is consistent with time periods used in other states for the maintenance of similar records and with the record keeping requirements of other businesses.

Subpart 2. **Report on devices stored in Minnesota.** Subpart 2 requires a licensee to report on a quarterly basis the gambling devices maintained under its control in Minnesota. The required information identifies the device and its location. The intent of the legislature in enacting Minnesota Statutes, section 299L.07, was to monitor and control the flow of gambling devices in Minnesota. As part of the regulatory plan, it is important for the department to know where gambling devices are stored in Minnesota. Quarterly reporting is established since it is consistent with other types of business reporting, such as tax reporting. Additionally, quarterly reporting narrows the time between the activity and the report to a reasonable, but not overly burdensome, schedule. Reporting of devices stored in Minnesota is only one part of the overall regulatory plan. These reports can be compared to the records obtained from other sources.

Subpart 3. **Report on devices shipped to Minnesota.** Subpart 3 requires a licensee to report shipments of devices into Minnesota. The information to be reported relates to the identity of the devices and parties involved in the shipment. As stated earlier, the intent of

the legislature in enacting Minnesota Statutes, section 299L.07, was to monitor and control the flow of gambling devices in Minnesota. The regulatory plan includes notice of shipments of gambling devices at the time of shipment. This reporting will keep the department current as to what devices are in the state and where they were sent. It is important that the information be submitted or mailed at or before the time of shipment so that the department can verify the accuracy of the information by inspections.

Subpart 4. Records required of licensed distributors of used devices. Subpart 4 requires that any person licensed to distribute used devices must have records to establish the age of devices held by the licensee. There is a substantial difference between the license fee for a distributor of new devices and the license fee for a distributor of used devices. The department needs to know the age of devices held by a licensee so the department can verify that the licensee holds the proper class of license.

7570.0040 INSPECTION OF LOCATION, RECORDS, AND DEVICES. Minnesota Statutes, section 299L.07, gives the commissioner authority to license and regulate manufacturers and distributors of gambling devices. As part of this authority, it is necessary for the commissioner to verify information submitted by a licensee and to verify compliance by the licensee with all laws and rules governing the licensee. Without verification, the commissioner cannot be sure of issuing a license that would not be detrimental to the effective regulation and control of gambling. See, Minnesota Statutes, section 299L.07, subdivision 3. It is reasonable to inspect the business premises, records, and devices of the licensee because this is limited to the things relevant to the license and to determining compliance. It is reasonable to not require advance notice of the inspection because this adds to the integrity of the inspection.

7570.0050 SUSPENSION AND REVOCATION OF LICENSE.

Subpart 1. Grounds for suspension or revocation. The enabling legislation, Minnesota Statutes, section 299L.07, subdivision 8, gives the commissioner authority to suspend or revoke a license. This subpart establishes the factors to be considered by the commissioner in making the decision to suspend or revoke a license. The factors all relate to the seriousness of the violations and are designed so that the commissioner is consistent with all licensees in applying suspension or revocation.

There are innumerable ways in which a licensee can violate the laws or rules governing the licensee, in addition to the varying levels of seriousness for each violation. For this reason, it is impossible to set out a rigid schedule of penalties to apply based on a specific list of violations. It is essential that the commissioner have the flexibility to address the violations that may occur. Requiring the commissioner to consider the factors listed in items A to F is a reasonable way to give the commissioner the necessary flexibility while at the same time limiting the discretion of the commissioner in a way that ensures fairness and consistency for all licensees. Additionally, the factors to be considered by the commissioner are similar to those used in taking license actions by the Minnesota Racing Commission in part 7897.0130, subpart 3.

Subpart 2. Grounds for summary suspension. The enabling legislation gives the commissioner authority to summarily suspend a license prior to a contested case hearing where necessary to ensure the integrity of gambling. This subpart sets out the factors to be considered by the commissioner in making the decision to summarily suspend a license.

The first factor to be considered is whether there are grounds for revocation of the license. This factor imposes a reasonable limitation on the commissioner because revocation is reserved for the most serious offenses and only the most serious offenses would threaten the integrity of gambling.

The second and third factors relate to assessing the risk of harm to the integrity of gambling and balancing this risk against the harm to the licensee of a summary suspension while a hearing is pending. It is reasonable that a summary suspension not be invoked for a trivial threat to the integrity of gambling. It is also reasonable to balance this risk against the potential harm to the licensee of a summary suspension because this harm is difficult to remedy if the hearing determines that a license revocation is not appropriate.

As discussed under subpart 1, establishing factors for the commissioner to consider in determining whether to summarily suspend a license is a reasonable way to give the commissioner the flexibility needed to address serious violations that may occur. At the same time, this limits the discretion of the commissioner in a way that ensures fairness and consistency for all licensees.

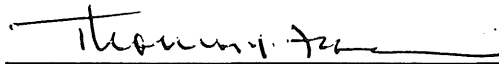
Subpart 3. **Procedures for suspension or revocation.** The Minnesota Administrative Procedure Act (APA) sets out minimum standards that must be followed for state agency actions such as license suspension or revocation. Subpart 3 refers to the APA so that all procedures for license withdrawal are set out in one place for the convenience of the reader.

Conclusion

Based on the foregoing, the Department's proposed rules are both necessary and reasonable.

11-23-92

Date


Thomas H. Frost, Commissioner
Department of Public Safety

OFFICE OF THE COMMISSIONER
211 Transportation Building
395 John Ireland Boulevard
Telephone: _____



STATE OF MINNESOTA
DEPARTMENT OF PUBLIC SAFETY
SAINT PAUL 55155-1889

December 3, 1992

Ms. Maryanne V. Hruby, Executive Director
Legislative Commission to Review Administrative Rules
55 State Office Building
100 Constitution Avenue
St. Paul, Minnesota 55155

Re: In the Matter of Proposed Rules of the State Department of Public Safety
Governing The Licensing Of Manufacturers And Distributors Of Gambling
Devices

Dear Ms. Hruby:

The Minnesota Department of Public Safety intends to adopt rules governing the licensing of manufacturers and distributors of gambling devices. We plan to publish a Notice Of Intent To Adopt Rules in the December 14, 1992, State Register.

As required by Minnesota Statutes, sections 14.131 and 14.23, the Department has prepared a Statement of Need and Reasonableness which is now available to the public. Also as required, a copy of this Statement is enclosed with this letter.

For your information, we are also enclosing a copy of the Notice Of Intent To Adopt Rules and a copy of the proposed Rules in this matter.

If you have any questions about these rules, please contact me at 296-2631.

Yours very truly,

A handwritten signature in cursive script that reads "Dave Orren".

Dave Orren
Rules Coordinator

enclosures: Statement of Need and Reasonableness
Notice Of Intent To Adopt Rules
Rules

The Legislative Commission to
Review Administrative Rules

DEC - 4 1992



