



Nez Perce

TRIBAL EXECUTIVE COMMITTEE

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May 30, 2017

Jonodev Chaudhuri, Chairman  
National Indian Gaming Commission  
1849 C Street N.W.  
Mail Stop #1621  
Washington, D.C. 20240

Re: 25 C.F.R. Part 547 – Grandfathered Class II Gaming Systems

Dear Chairman Chaudhuri:

The Nez Perce Tribe (Tribe) offers the following comments on the “grandfathering” provision in the National Indian Gaming Commission’s (NIGC) Class II Technical Standards, 25 C.F.R. Part 547. In particular, the Tribe wishes to comment on the “sunset clause” within the grandfathering provision, which provides that certain Class II gaming systems manufactured before November 10, 2008, must either be brought into compliance with the requirements of 25 C.F.R. Part 547 or removed from play.

As an initial matter, we would like to express our appreciation and support for the NIGC’s efforts to reach out and consult with tribal governments on this issue, which has long been a source of concern for both tribal governments and the NIGC alike. As acknowledged by the NIGC, the issue of grandfathered Class II gaming systems, “more than any other topic, has been the subject of long deliberation and analysis within the Commission.”<sup>1</sup> Tribal governments have similarly invested significant time and effort to better understand the impact of the sunset clause on tribal gaming operations.

In fact, earlier this year, a Class II Gaming Sub-Committee (Class II Sub-Committee) consisting of tribal regulators and other Class II gaming experts was commissioned by the National Indian Gaming Association to collect data concerning the technical performance of grandfathered Class II gaming systems. With the assistance of the research firm KlasRobinson, a survey was conducted across Indian Country to determine the quantitative impact of the sunset clause and the level of risk, if any, posed by grandfathered systems on the integrity and security of Class II gaming.

The survey included the participation of 32 tribal governments representing 117 tribal casinos in 12 different states. Of the participants, 18 tribes operating approximately 16,040 grandfathered

Class II gaming systems in 93 casinos across 7 states, provided input on the integrity, safety, and security of their grandfathered games. Approximately 15,750 of the 16,040 grandfathered gaming systems surveyed were operated by Oklahoma tribes.

As discussed below, the survey found no evidence whatsoever to indicate or even suggest that grandfathered Class II gaming systems are any less secure or more susceptible to a breach than their fully compliant counterparts. The Tribe believes the survey results and findings provide the evidentiary basis needed to show that the sunset clause is neither appropriate nor justified and should be withdrawn from 25 C.F.R. Part 547. We hope that the NIGC will take the survey results and our comments below into due consideration and work to resolve this long-standing issue in a manner that will ensure the preservation and continued growth of the Class II gaming industry.

**1. GRANDFATHERED CLASS II GAMING SYSTEMS DO NOT POSE ANY RISK TO GAMING OPERATIONS OR PATRONS AND ARE NO LESS SECURE THAN FULLY COMPLIANT CLASS II GAMING SYSTEMS.**

It has been nearly a decade since the grandfathering provision was first introduced by the NIGC for the purpose of “avoid[ing] any potentially significant economic and practical consequences of requiring immediate compliance”<sup>ii</sup> with the then-new Technical Standards. During the rulemaking preceding the 2008 final rule of 25 C.F.R. Part 547, one commenter suggested exempting all existing Class II gaming technology from the Technical Standards, to which the NIGC replied:

Perpetually grandfathering existing hardware will create a permanent class of non-compliant equipment. That is not consistent with the regulatory purpose of the technical standards, namely to ensure the integrity and security of Class II gaming systems and the accountability of Class II gaming revenue.<sup>iii</sup>

No further analysis or discussion was or has since been provided to support the NIGC’s conclusion that a permanent exemption of grandfathered games would somehow be inconsistent with the regulatory purpose of 25 C.F.R. Part 547. But an extreme measure such as the wholesale removal of a gaming product from the marketplace demands a compelling justification based on adequate facts and information. With less than two years remaining until the sunset deadline, the need to establish a rational connection between the regulatory purpose of the sunset clause and grandfathered gaming systems is more pressing now than ever before.

The first step in establishing this connection is to determine the regulatory benefits, if any, in bringing all gaming systems into full compliance with 25 C.F.R. Part 547. Or, put conversely, identifying the regulatory detriments that would result from the continued operation of grandfathered games past the sunset deadline. Before the sunset clause takes effect, it should be undeniably clear that the mandatory retirement of grandfathered gaming systems will make Class II gaming safer and more secure. The non-compliant status of grandfathered systems, standing alone, is not a sufficient basis upon which to mandate a recall of lawful gaming equipment.

Moreover, if the regulatory objective of 25 C.F.R. Part 547 is to ensure the integrity and security of Class II gaming systems, there must be some evidence to support the NIGC’s position that maintaining grandfathered games past the sunset deadline will somehow impede achievement of this objective. Since even the most highly regulated gaming activity is subject to some degree of

risk, the evidence must show that grandfathered gaming systems are subject to *increased* risks relative to their fully compliant counterparts.

The survey commissioned by the Class II Sub-Committee was focused on gathering information on the above issues, relying on the experiences and knowledge acquired by Class II gaming tribes. Of the 93 casinos with grandfathered systems that were surveyed, not one reported any breaches of safety, security, or integrity during operation, or believed that grandfathered systems were susceptible to cheating or manipulation by patrons. Survey participants did, however, report a few, albeit very minimal, compliance issues with fully compliant systems. Though few in number, they nonetheless exceed the number of compliance issues reported with respect to grandfathered systems. Based on their experiences, all 93 casinos unanimously agreed that there are no technical or commercial reasons why grandfathered systems could not be offered after the sunset deadline of November 10, 2018.

In the nearly ten years since the promulgation of the grandfathering provision, we have not been made aware of any documented instances where a grandfathered system posed a greater risk to patrons or the tribal gaming operation than a fully compliant gaming system. As confirmed by the survey results, there is simply no basis for concluding that the removal of grandfathered Class II gaming systems will make Class II gaming any safer or more secure. The mere fact that a system is fully compliant with 25 C.F.R. Part 547 does not seem to bear any regulatory benefits with respect to the safety, security, or integrity of Class II gaming. Therefore, full compliance with the Technical Standards, while important, is not a necessary condition to achieving the NIGC's stated regulatory objectives.

Moreover, experience has shown that grandfathered gaming systems are no less technically advanced or secure than fully compliant systems. In fact, some game manufacturers provide grandfathered systems that are more advanced and secure than what is required by 25 C.F.R. Part 547 and tribal regulators. It should also be noted that tribal regulatory gaming authorities have been exercising their authority as the primary regulators of Class II gaming to evaluate and approve modifications that have improved the overall performance and compliance of grandfathered Class II gaming systems.

In the absence of any identified risks or threats, a rational connection cannot be drawn between the sunset clause and the regulatory purpose of 25 C.F.R. Part 547. There are no facts or evidence to support a hard sunset deadline, nor does the historical record of Class II gaming support the NIGC's proposition that the operation of grandfathered games will compromise the safety, security, or integrity of Class II gaming.

Given that grandfathered systems have been operating for over a decade without any safety or integrity issues, a blanket recall of such products from the market would constitute an arbitrary and capricious act. We can think of no administrative agency, including those with specific statutory authority to promulgate product standards, that would require a general recall of products in the marketplace without a showing of a defect or flaw that poses an imminent threat to human life or safety. The survey findings did not reveal any defects, flaws, or threats – technical or otherwise – in relation to grandfathered systems that would warrant a product recall.

However, even assuming, *arguendo*, that grandfathered gaming systems did somehow pose a higher risk to patrons or the gaming operation than fully compliant systems, such risks would be continuously mitigated and avoided through the monitoring and enforcement functions of tribal gaming regulatory authorities. The day-to-day, frontline regulation of tribal gaming is performed by tribal gaming regulatory authorities, who possess both the knowledge and technical expertise to immediately identify, assess, and mitigate any potential or actual threats and risks to the gaming operation. As the primary regulators of Class II gaming, tribal gaming regulatory authorities should be fully accorded that role in the NIGC's regulations, especially those governing Class II gaming activities such as 25 C.F.R. Part 547.

## **2. IMPLEMENTATION OF THE SUNSET CLAUSE WILL CAUSE SIGNIFICANT ECONOMIC HARM TO THE CLASS II GAMING INDUSTRY AND THE TRIBAL GOVERNMENTS WHO RELY ON CLASS II GAMING REVENUE AS AN IMPORTANT ECONOMIC BASE.**

In the consultation briefing materials provided to us earlier this year, the NIGC included a background discussion of the grandfathering provision, which noted the "particular concern" at the time the regulation was promulgated of "the potential financial burden on bringing gaming systems that had already been manufactured and/or put into play . . . into compliance with the new 2008 rule."<sup>iv</sup> As explained by the NIGC, the grandfathering provision was enacted to "reduce that cost"<sup>v</sup> to tribal governments.

If the intent of the grandfathering provision is to mitigate the costs of compliance to tribal governments, it is unclear why it still includes a sunset requirement that is certain to cause significant economic harm without generating any appreciable regulatory benefits. The financial hardship on tribes should not be any less of a concern today than it was when the grandfathering provision was first enacted in 2008.

The negative economic impact of the sunset clause will be immense and jeopardize the economic viability of the Class II gaming industry, which is of vital importance to tribal governments not just financially, but also as an aspect of tribal sovereignty and economic development. Grandfathered Class II gaming systems represent a large percentage of the total Class II gaming systems in play nationally. To provide a sense of scale, in Oklahoma alone, there are approximately 24,000 grandfathered Class II gaming systems, which constitute roughly 41% of all Class II gaming systems in operation nationwide. Implementation of the sunset clause would wipe out nearly half of the Class II gaming systems across Indian Country.

When calculating the compliance costs associated with the sunset clause, it is important to bear in mind that the economic costs to tribal governments will go beyond the direct costs of replacing grandfathered equipment. First, there is the loss of the tens of millions of dollars that have been invested by tribal governments in purchasing and maintaining grandfathered gaming equipment and technology. There are also the costs associated with the downtime required to upgrade or replace grandfathered systems, which could take up to 30 days or longer. The loss of play and visitation by patrons who prefer the retired grandfathered games would also cause serious economic harm to those tribal governments who rely on grandfathered games as a major source of tribal revenue.

We note that at the time the grandfathering provision was enacted, the NIGC's belief was "that natural market forces" would phase out existing Class II gaming technology, and that the "looming sunset of the grandfather period would otherwise incentivize the industry's transition to fully compliant systems."<sup>vi</sup> It appears the NIGC predicted that these events would help mitigate the costs associated with replacing grandfathering equipment. However, this has not proven to be the case; in fact, the opposite result has occurred, as confirmed by the survey results.


Survey participants with grandfathered games unanimously reported that their grandfathered Class II gaming systems are still profitable for their casinos, and that none of their patrons are demanding that they be replaced with more modern machines. One participant commented that "some of the grandfathered games have the highest following among any of the offered games." For one tribe, the "Class 2 grandfathered games earn the most revenue per day per device." As expected, the survey confirmed that grandfathered gaming systems not only have a loyal customer base, but are in some instances preferred over newer games that lack the familiar look and feel that patrons expect.

Thus, none of the predicted cost-mitigating events appear to have occurred. Contrary to the NIGC's predictions, market forces have actually supported rather than stymied the continued operation and economic viability of grandfathered Class II gaming systems. Given their popularity and profitability, there is no real incentive – financial or otherwise – for tribal gaming operations to even begin considering the replacement of grandfathered gaming systems for fully compliant ones. The financial burden that was of "particular concern" in 2008 has not lessened, but rather increased exponentially and should be at the forefront of the NIGC's deliberations.

### 3. CONCLUSION

In closing, the Tribe thanks the NIGC for the opportunity to share our views and concerns regarding the grandfathering provision in 25 C.F.R. Part 547. We again urge the NIGC to reconsider its approach to the sunset clause, which will have serious consequences on the economic well-being of tribes and their interdependent industries. The goal should be to reduce or avoid unnecessary compliance costs, without sacrificing the benefits of regulation. Where, as here, there are no demonstrable benefits of regulation associated with the sunset clause, there is simply no basis or justification for mandating the retirement of lawful, profitable, and secure gaming systems.

Sincerely,



Mary Jane Miles  
Chairman

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<sup>i</sup> Minimum Technical Standards for Class II Gaming Systems and Equipment, 77 Fed. Reg. 58475 (Sept. 21, 2012).

<sup>ii</sup> Technical Standards for Electronic, Computer, or Other Technologic Aides Used in the Play of Class II Games, 73 Fed. Reg. 60,508, 60,521 (Oct. 10, 2008) (to be codified at 25 C.F.R. pt. 547).

<sup>iii</sup> *Id.* at 60,521.

<sup>iv</sup> NIGC Consultation Briefing 2017, pg. 7, available at <https://www.nigc.gov/images/uploads/2016-12-12%20Consultation%20Briefing%20clean.pdf>.

<sup>v</sup> *Id.*

<sup>vi</sup> *Id.*