STATE OF NEBRASKA
Office of the Attorney General
2115 STATE CAPITOL BUILDING
LINCOLN, NE 68509-8920
(402) 471-2682
TDD (402) 471-2682
FAX (402) 471-3297 or (402) 471-4725

DOUGLAS J. PETERSON
ATTORNEY GENERAL

SUBJECT: Interpretation of LB 70 as Amended – Imposition of an Additional Occupation Tax Under the Mechanical Amusement Device Tax Act for Certain Devices.

REQUESTED BY: Senator Jim Smith
Nebraska Legislature

WRITTEN BY: Doug Peterson, Attorney General
L. Jay Bartel, Assistant Attorney General

The Mechanical Amusement Device Tax Act, Neb. Rev. Stat. §§ 77-3001 to 77-3011 (2009) [the "MAD Tax Act"], imposes an occupation tax on the business of operating mechanical amusement devices within the State of Nebraska. The tax is due and payable on January of each year on each machine or device in operation on that date, or before the time the machine or device is placed in operation for machines or devices put into operation after January 1. Neb. Rev. Stat. § 77-3004(2) (2009). Currently, the occupation tax is thirty-five dollars for each machine or device in operation on January 1, and twenty-five dollars for machines or devices placed in operation after July 1 of the tax year. Neb. Rev. Stat. § 77-3004(4) (2009). "Mechanical amusement device" is defined to include "any machine which, upon insertion of a coin, currency, credit card, or substitute into the machine, operates or may be operated or used for a game, contest, or amusement of any description ...." Neb. Rev. Stat. § 77-3001(2) (2009). "[D]evices that are mechanically constructed in a manner that would render their operation illegal under the laws of the State of Nebraska..." are excluded from the definition of "mechanical amusement device." *Id.*

LB 70, as originally introduced, authorized a city or village to levy an additional occupation tax on the business of operating mechanical amusement devices awarding a monetary price or anything redeemable for a monetary prize within the boundaries of the city or village, or, for devices operated outside a city or village, authorized a county

to levy an additional occupation tax. LB 70, § 2(1). The amount of the additional occupation tax was ten percent of gross revenue derived from operation of the devices. LB 70, § 2(2). The committee amendment to LB 70 (AM118) eliminated the local tax authorized in the original bill, and instead provided that the additional tax of ten percent of gross revenue derived from operation of machines or devices subject to the tax was to be collected by the Tax Commissioner concurrently with the state sales tax. AM 118, § 2(3). The amendment further limited application of the additional occupation tax, providing that it was to be levied

> upon the business of operating a mechanical amusement device that:
>
> (a) Accepts currency, coins, tokens, or other value in exchange for play;
>
> (b) Awards a monetary prize or anything redeemable for a monetary prize;
>
> (c) Is played by a player using a touch screen, computer mouse, touch pad, light pen, laser, or device of similar function by which the player competes against software running the device; and
>
> (d) Has not been adjudicated by a court of competent jurisdiction within the State of Nebraska to not constitute a gambling device as defined in subdivision (5) of section 28-1101. Any such adjudication shall be by way of a final order in which the Tax Commissioner has been made a party to the action and written notice shall have been provided to the Attorney General at the commencement of the action. AM 118, § 2(1).

AM 118 also limited the circumstances under which an operator subject to the additional occupation tax could demonstrate a mechanical amusement device was not subject to the tax, providing:

> If an operator believes that a mechanical amusement device is not subject to [the additional occupation tax imposed] under subsection (1) of this section, the burden is on the operator to prove to the Tax Commissioner that such device does not have one or more of the characteristics required for taxability under subsection (1) of this section. Such proof may be made by, among other things, a showing that the software running the game remains constant with the nature of a game that had its software at issue in a judicial case, not overturned by appeal, in which the State of Nebraska was party, the issue was litigated, and the final order found that the particular game is more controlled by the player than not, and thus is predominately a game of skill. AM 118, § 2(2).

AM 118 also provided that the additional occupation tax "shall not apply to any device not within the definition of a gambling device as defined in subdivision (5) of section 28-1101 or to any device that is specifically authorized by law." AM118, § 2(5). AM 118 was adopted and has been placed on Select File with ER 27.

You have asked for our opinion on two questions regarding the interpretation of LB 70 as amended. In addition, you have requested our view on potential legal ramifications of the bill on the prosecution of cases involving potentially illegal gambling devices. Your questions, and our responses, are set out below.

1. **Section 2(1)(d) limits application of the tax to those devices that have "not been adjudicated...to not constitute a gambling device...." First, how do you interpret this provision? Second, does this provision exempt from the new tax those devices which were adjudicated in *American Amusements Co. v. Nebraska Department of Revenue,* 282 908, 807 N.W.2d 492 (2011)? I am concerned that the language appears to exempt the devices at issue in that case in their entirety even though the court only found that certain games on the devices were legal. Is that correct?**

Section 2(1)(d) imposes the additional occupation tax on any mechanical amusement device that "[h]as not been adjudicated by a court of competent jurisdiction within the State of Nebraska to not constitute a gambling device as defined in subdivision (5) of section 28-1101." This subsection further provides: "Any such adjudication shall be by way of final order in which the Tax Commissioner has been made a party to the action and written notice shall have been provided to the Attorney General at the commencement of the action."

"Statutory language is to be given its plain and ordinary meaning in the absence of anything indicating to the contrary." *PSB Credit Services, Inc. v. Rich,* 251 Neb. 474, 477, 558 N.W.2d 295, 297 (1997). The plain language of § 2(1)(d) provides that a mechanical amusement device subject to the additional occupation tax is one that meets the criteria in subsections (a) through (c) (accepts currency, coins, tokens, or other value in exchange for play, awards a monetary prize or anything redeemable for a monetary prize, and is played by a player using a touch screen, computer mouse, touch pad, light pen, or device of similar function by which the player competes against software running the device), and has not been adjudicated by a Nebraska court to not constitute a gambling device as defined in § 28-1101(5). Further, that adjudication must be by a final order in a case where the Tax Commissioner has been a party and the Attorney General received written notice when the action was commenced.

The only device that would currently be excluded under § 2(1)(d) is the Bankshot game at issue in *American Amusement Co. v. Nebraska Dep't of Revenue,* 282 Neb. 908, 807 N.W.2d 492 (2011) ["*American Amusements*"]. *American Amusements* involved whether a video game called "Bankshot" was an unlawful game of chance and thus an illegal gambling device. The game could be played in various modes (Spin, Slow, and Fast), and included certain bonus and jackpot prizes. The Nebraska Supreme Court affirmed the district court's finding that the Bankshot game, when played in the Spin mode, was not a game of chance, as, in this version, the game "was more controlled by the player than not, and thus [was] predominately a game of skill." 282 Neb. at 925, 807 N.W.2d at 504. The district court found that the outcome of the Bankshot game, when played in the Slow mode, was determined predominately by

chance, and thus was illegal gambling. *Id.* at 914, 807 N.W.2d 497. The district court found neither party carried its burden to prove the nature of the game in Fast Mode, and thus made no decision on whether the game was gambling in this mode. *Id.* In addition, the district court determined that Bankshot's pool bonus and jackpot were not gambling in the Spin mode, but were gambling in the Slow mode, and that both the Fast Break Bonus and the Speed Break bonus were gambling. *Id.* No cross-appeal was taken from the district court's findings "that (1) the Speed Break and Fast Break bonus games of Bankshot [were] games of chance; [and] (2) Bankshot when played in the Slow mode [was] a game of chance..." *Id.* at 916, 807 N.W.2d at 498. Further, the Fast Mode of play was eliminated following the district court decision and was not at issue before the Supreme Court. *Id.* Thus, the only question presented to the Supreme Court was "whether the district court properly found that Bankshot [was] not a game of chance when played in Spin mode." *Id.* at 916, 807 N.W.2d at 498-99.

The Bankshot device would not fall within the parameters established in § 2(1)(d), as it was adjudicated by a final order of the Supreme Court to not be a game of chance, and thus not an illegal gambling device under § 2-1101(5). Also, the Tax Commissioner was a party in *American Amusements*, and the Attorney General obviously had written notice of the case at its commencement, as the Attorney General was also made a party to that litigation. While the Bankshot game adjudicated in *American Amusements* would be a device satisfying the criteria for exclusion from the tax set forth in § 2(1)(d), only the version of the game in Spin mode was held not to constitute a game of chance and thus not an illegal gambling device.

"If possible, a statute should be construed in such a way as to negative any constitutional infirmity." *Prendergast v. Nelson,* 199 Neb. 97, 111, 256 N.W.2d 657, 667 (1977). Construing § 2(1)(d) to remove from taxation those versions of the Bankshot game that were found to constitute a game of chance must be avoided, as it would attempt to authorize illegal conduct. Such an interpretation cannot be adopted if a permissible construction can be made which does not produce such a result. Section 2(1)(d) thus must be interpreted to exclude from taxation only the Bankshot game in the Spin mode, as that is the only version of the game that has been adjudicated by final court order not to constitute a game of chance or illegal gambling device. Accordingly, we do not interpret this provision to exempt from taxation the other versions of the Bankshot game that were either found to be impermissible games of chance (the Slow Mode and the Speed Break and Fast Break Bonus), or were not the subject of a final adjudication as to whether the game was predominately chance or skill (the Fast mode).

2. **When subsection (d) is read together with Section 2(2), does it exempt from the new tax not only those devices adjudicated in *American Amusements*, but all present or future devices which are programmed with software of the "same" nature as those devices? Is there any existing statutory or case law which would inform or direct the Tax Commissioner as to what constitutes software that remains constant with "the nature" of software previously adjudicated by a court?**

Subsection 2(2) provides the operator of a mechanical amusement device must pay the additional occupation tax unless the operator can prove the device is not subject to the tax because it does not have one or more of the characteristics making it taxable under subsection (1). This "proof may be made by, among other things, a showing that the software running the game remains constant with the nature of a game that had its software at issue in a judicial case, not overturned by appeal, in which the State of Nebraska was a party, the issue was litigated, and the final order found that the particular game is controlled more by the player than not, and thus is predominately a game of skill." § 2(2).

Construed with § 2(1)(d), this subsection would exempt the Bankshot game in Spin mode and any version of the game using software which runs "constant" with that version of the game. We have no way of knowing if other devices could be programmed with software of the same "nature" within the meaning of § 2(2). No further definition or explanation of the terms used in § 2(2) is provided, nor are we aware of any statute or case law which would aid in construing the proof requirement articulated in this subsection. If called on to interpret this provision, the Tax Commissioner would have to determine if the software running a device an operator believes falls under this subsection is "constant with the nature of a game" in which the software was found not to constitute a game of chance, which presently includes only the Bankshot game in Spin mode. Also, it is unclear if other games could use software of the same "nature" as Bankshot, as the Bankshot software may well be proprietary and not available to other game manufacturers or distributors.

3. **Finally, are there any legal ramifications with regard to the state's ability to litigate future cases involving gaming devices by adopting the language in LB 70? Simply put, would LB 70 impede the Legislature's ability to regulate gaming in the state?**

We understand your final question as asking if imposition of the additional occupation tax imposed under LB 70, as amended, would sanction or legalize devices or machines which are subject to the tax, even if those devices or machines may constitute games of chance or illegal gambling devices under § 28-1101(5), but their legality has not been judicially determined. For several reasons, the bill does not, and cannot, have that effect.

The definition of mechanical amusement device in the MAD Tax Act specifically excludes "devices which are mechanically constructed in a manner that would render

their operation illegal under the laws of the State of Nebraska." Neb. Rev. Stat. § 77-3001(2) (2009). The mere presence of a decal signifying payment of the occupation tax required under the MAD Tax Act does not legitimize machines or devices that are otherwise unlawful gambling devices, and such machines or devices are subject to forfeiture. *See State v. Two IGT Video Poker Games,* 237 Neb. 145, 147, 465 N.W.2d 453, 456 (1991) (Noting machines seized and ordered forfeited as illegal gambling devices "had affixed to them mechanical amusement device stickers from the Nebraska Department of Revenue."). Just as affixing a MAD Tax decal to an illegal gambling device does not make the device legal, assessment and payment of the additional occupation tax imposed by LB 70 as amended would not be determinative of the legality or illegality of any machine or device upon which the tax is assessed and paid. Indeed, a tax is imposed on marijuana and other controlled substances possessed by dealers under the Marijuana and Controlled Substances Tax Act, Neb. Rev. Stat. §§ 77-4302 to 77-4316 (2009). The imposition of a tax on dealers possessing marijuana and other controlled substances, and subjecting dealers who fail to pay the tax and affix the required stamps on all marijuana and controlled substances to penalties for noncompliance, does not legalize possession of these drugs by dealers, who would still be subject to prosecution for violation of criminal statutes related to illegal drug possession.

Unlike the tax imposed on marijuana and other controlled substances under §§ 77-3402 to 77-4316, however, which can apply only to drugs that are illegal and subject to criminal sanction, the additional occupation tax imposed under LB 70 as amended applies to any device that falls within the criteria in § 2(1)(a)-(d), even though the device may or may not constitute a game of chance or be an illegal gambling device. The Committee Records on LB 70 indicate a concern that machines that "may well be unlawful..." have been placed in operation subsequent to the decision in *American Amusements*. Committee Records on LB 70, 104th Leg., 1st Sess. 1 (Jan. 23, 2014). The Introducer's Statement of Intent further states that, with respect to imposition of the additional occupation tax, the intent is to "place the burden of proof on the operator to establish the lawfulness of the game and entitlement to exemption from the tax." *Id.*, Introducer's Statement at 1.

Section 2(5) of the bill provides: "The occupation tax imposed in this section shall not apply to any device not within the definition of a gambling device as defined in subdivision (5) of section 28-1101 or to any device that is specifically authorized by law." Thus, under this subsection, the tax is not to be imposed on any device that is not unlawful under § 28-1101(5). Other than the limited exclusion in § 2(1)(d) for devices that meet the requirements of subsections (a) through (c) and have been "finally adjudicated" to not constitute an illegal gambling device (which is limited to a single device), or devices using software that "remains constant with the nature of a game" judicially determined not to be a game of chance (again limited to a single game or device), there is no mechanism in the bill for an operator to seek exemption from the additional occupation tax by establishing a particular machine or device is not illegal under § 28-1101(5).

"Because exaction of a tax constitutes a deprivation of property, the State must provide procedural safeguards against unlawful exactions in order to satisfy the demands of the Due Process Clause." *McKesson Corp. v. Division of Alcoholic Beverages and Tobacco,* 496 U.S. 18, 36 (1990) ["*McKesson*"]. "A state has flexibility to provide [a] remedy before the disputed taxes are paid (predeprivation), after they are paid (postdeprivation), or both." *Reich v. Collins,* 513 U.S. 106, 108 (1994). If taxpayers are not provided "with a meaningful opportunity to withhold payment and to obtain a predeprivation determination of the tax assessment's validity...", taxpayers can be required "to raise their objections in a postdeprivation refund action." *McKesson*, 496 U.S. at 38. "To satisfy the requirements of the Due Process Clause...", the refund action "must provide taxpayers with, not only a fair opportunity to challenge the accuracy and legal validity of their tax obligation, but also a 'clear and certain remedy,"..., for any erroneous or unlawful tax collection to ensure the opportunity to contest the tax is a meaningful one." *Id.* at 38-39 (citation omitted).

Apart from proving to the Tax Commissioner that a machine or device does not satisfy one or more of the criteria in § 2(1)(a) to (d), including demonstrating the game software is constant with the nature of a game adjudicated to be lawful under § 2(2), LB 70 as amended provides no mechanism for an operator to seek a determination by the Tax Commissioner that a machine or device is not a gambling device as defined in § 28-1101(5) and thus not subject to the additional occupation tax. While such a pre-deprivation remedy is not constitutionally required if an adequate post-deprivation remedy exists, the bill could be amended to permit an operator of a machine or device to make a showing to the Tax Commissioner that a device is legal and thus should be exempt from imposition of the additional tax. If the Tax Commissioner found that showing to be insufficient, the operator could be provided an opportunity for an administrative hearing to present evidence that a machine or device is lawful and not subject to the additional occupation tax, after which the Tax Commissioner would enter a final decision either approving or denying the exemption. If denied, the Tax Commissioner's final decision would be appealable under the Administrative Procedure Act ["APA"] as a final decision in a contested case. *See* Neb. Rev. Stat. § 84-901(3) and 84-917 (2014).[1]

---

[1] Rather than imposition of an additional tax on devices of the type LB 70 intends to reach, an alternative would be to require that, prior to an operator being issued a decal or sticker to permit use of the device as a mechanical amusement device, the operator be required to make a showing of the legality of the game to the Tax Commissioner. The administrative process could provide for a hearing in the event the Tax Commissioner initially disapproves an application for permission to use the device, and a final decision subject to appeal if the application is denied. A process of this nature would require a showing a device is a lawful mechanical amusement device prior to issuance of the required MAD Tax decal or sticker. The purpose and focus of this process is regulation, rather than additional taxation.

If no pre-deprivation remedy is provided, a person paying the additional tax must be afforded a post-deprivation procedure to contest imposition of the tax. Neither LB 70 as amended nor the MAD Tax Act currently contain a specific refund process. The Legislature has, however, established a procedure for taxpayers to seek refunds of taxes collected by the Tax Commissioner where no specific refund provision has been enacted. Neb. Rev. Stat. §§ 77-1777 to 77-1782 (2009). Under this procedure, a taxpayer can file a written claim for refund with the Tax Commissioner, and request a hearing before the Tax Commissioner prior to action on the refund claim. Neb. Rev. Stat. §§ 77-1779 and 77-1780 (2009). If the claim is denied, the taxpayer can appeal the denial pursuant to the APA. Neb. Rev. Stat. § 77-1781 (2009). While this remedy presumably would be available, it may be advisable to amend LB 70 to adopt a specific refund remedy.

Very truly yours,

DOUG PETERSON
Attorney General

L. Jay Bartel
Assistant Attorney General

Approved by:

Attorney General

pc Patrick J. O'Donnell
Clerk of the Nebraska Legislature

07-920-29