Executive Summary of Sunset Staff Report | Texas Lottery Commission

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The Texas Lottery Commission (TLC) is stuck between a rock and a hard place. Two of the state's forms of legalized gaming — the lottery and charitable bingo — exist to raise revenue primarily for education and charities, respectively. However, the law requires TLC to exercise strict control and close supervision over both games, which can negatively impact revenue generation. Furthermore, the agency must accomplish these tasks through an outdated statute and in an environment where many oppose gaming altogether. In response to this dilemma, TLC is becoming stagnant. Having found a way to be successful at its most visible function, raising revenue, the agency has been unwilling or unable to adapt to a changing environment or fully embrace some of its regulatory responsibilities. TLC's history with the Sunset process has never been smooth sailing, due in part to gaming-related issues that lie completely outside Sunset staff's scope. In 2003 and 2005, the Legislature did not pass the agency's Sunset bill and instead continued it through separate legislation. In 2013, the bill nearly suffered the same fate but was eventually passed. More than a decade later, this Sunset review occurs amid criticism by some for TLC's stance on lottery courier companies — an unregulated and controversial business model that now accounts for an estimated 9 percent of TLC's draw ticket sales. The issue epitomizes the challenge the agency faces trying to balance the state's interest in raising revenue and regulating the lottery and bingo.

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Population growth, changes in consumer preferences, and rapid technological advancements all affect both the lottery and bingo. As with previous reviews of TLC, Sunset staff did not consider policy issues directly linked to these changes, such as gaming expansion or whether the state should regulate or prohibit lottery couriers. Instead, this review focused on how the agency navigates and addresses these challenges. To do that effectively, TLC needs an active, involved commission that provides staff guidance and direction while ensuring the agency fully meets its regulatory responsibilities. However, the commission has not risen to the challenge. The commission often plays a passive role in critical functions like planning and rulemaking, leaving the agency with no clear vision for its future and struggling to adapt to current circumstances. To this end, Sunset staff recommendations focus on increasing the commission's participation in key agency policymaking functions and providing it mechanisms to proactively bring forward concerns to the Legislature.

Regarding its oversight of the lottery, agency staff does a good job managing its long-time lottery operations contractor. However, the commission is overly reliant on its contractor and staff to understand the industry and is missing opportunities for gathering and considering broader input on overlooked or contentious topics.

On the bingo side of the house, TLC's sole responsibility is to ensure the game is fair and proceeds are accurately disbursed. While bingo does make money for all involved — charities, bingo operators, the state, and local governments — the state continues to regulate bingo because it is a cash-based enterprise with very real opportunities for fraud. Unlike the lottery, TLC has no authority or obligation to promote bingo; its only purpose is to regulate the industry. However, Sunset staff has consistently identified problems with the agency's bingo regulation, and this review was no exception. Operational inefficiencies such as disjointed information technology (IT) systems, inadequate inspection criteria, limited training, and poor data management leave TLC struggling and raise questions as to whether the agency can effectively regulate bingo. In an attempt to make lasting improvements, the recommendations seek to not only address these specific concerns but also make more significant changes to bingo's unusual statutory leadership structure and regulatory scheme. For example, specifying that the executive director rather than the commission employs the Charitable Bingo Operations Division (CBOD) director would correct a failed experiment in bifurcated leadership and create a single chain of command within the agency to effectively regulate bingo. Recommendations to eliminate two licenses and options to consolidate two others would eliminate unnecessary burdens on certain regulated businesses.

About halfway through the Sunset review, TLC's long-time executive director retired. Just before publication of this report, the commission named its former deputy executive director as the agency's new administrative head. This leadership change provides the perfect opportunity for TLC to revitalize its efforts to address the shortcomings in bingo regulation and prepare the agency to deal with future challenges.

The following material summarizes Sunset staff's recommendations on the Texas Lottery Commission.

Sunset Staff Issues and Recommendations

Issue 1

The Agency's Governing Body Is Not Adequately Engaged and Lacks Mechanisms to Ensure the Long-Term Success of the State Lottery and Charitable Bingo.

The commission does not provide adequate guidance or direction for key agency functions and is not actively involved in developing the agency's overarching mission, goals, and major initiatives. Despite previous Sunset Commission recommendations to increase commission involvement through subcommittees, members have adopted a ministerial approach to their oversight responsibilities by approving rules and key planning documents with limited involvement, discussions, or questions. The commission also needs better mechanisms to stay informed about the rapidly changing lottery and bingo industries and would benefit from a more effective Bingo Advisory Committee as well as a formal Lottery Advisory Committee. Additionally, a more cohesive reporting requirement would provide the commission and Legislature with a comprehensive overview of the agency's two primary functions and potential industry challenges.

Key Recommendations

- Require the commission to establish subcommittees to improve opportunities for engagement and update its policies describing the separation of duties between commission and staff.

- Modify statute to require the Bingo Advisory Committee and improve its effectiveness.

- Require the commission to establish a Lottery Advisory Committee.

- Consolidate four of TLC's reporting requirements into a new *Texas Lottery Commission Annual Report*.

- Direct TLC to evaluate and address gaps in its rules.

ISSUE 2

The Charitable Bingo Operations Division Needs Significant Improvements to Ensure Effective, Fair, and Efficient Bingo Regulation.

Structural barriers and operational inefficiencies within TLC impede the effective regulation of charitable bingo. TLC's funding structure, where lottery funds subsidize bingo regulation, potentially violates statutory requirements. Additionally, TLC's unusual leadership structure, with the TLC executive director and the CBOD director both reporting directly to the commission, contributes to administrative complexities and inefficiencies. Establishing an indirect administration goal in the agency's budget and restructuring its organizational hierarchy would ensure full compliance with the State Lottery Act and help streamline agency functions under a single chain of command. Furthermore, CBOD remains entangled in paper-based processes, straining its limited financial resources and staff time. Additionally, the lack of clear bingo inspection criteria coupled with insufficient training results in potentially incomplete inspections and inconsistent treatment of licensees. Prioritizing IT updates and improving data practices and staff training would enhance efficiency while improving the fairness and effectiveness of bingo regulation.

Key Recommendations

- The House Appropriations and Senate Finance committees should consider modifying TLC's budget pattern to include an indirect administration goal.

- Modify statute to clarify TLC's organizational hierarchy.

- Direct the agency to establish a plan prioritizing IT updates and eliminating paper-based processes in CBOD.

- Direct the agency to improve data practices, including data validation and other quality controls.

ISSUE 3

Charitable Bingo Licensing Needs Changes to Eliminate Unnecessary Regulatory Burdens and Unfair Advantages to Certain Regulated Businesses.

Sunset staff identified two license types that do not meet the need for continued regulation and two others for which Sunset staff provides options for consolidation. Bingo manufacturers licenses are no

longer necessary as TLC has adopted standards for bingo materials that effectively regulate manufacturers without licensure. Licensing distributors of bingo materials does not provide any additional benefit in ensuring the integrity of bingo games. TLC's current regulatory scheme creates and preserves an unfair preferred class of lessor, as grandfathered lessors may earn up to three times as much rent as a regular lessor. A recommendation to preserve or eliminate these special rights cannot be made without wading into policy issues; therefore, this report provides options for the Sunset Commission's consideration.

Key Recommendation

- Eliminate the licenses for manufacturers and distributors of bingo materials.

Proposed Options

Option 1. Treat all lessors as grandfathered lessors.

Option 2. Convert all grandfathered lessors to regular lessors.

Issue 4

The State Has a Continuing Need for the Texas Lottery Commission.

TLC has operated the lottery since 1993 and regulated charitable bingo since 1994. Lottery is popular in Texas, generating record sales in each of the last 13 years, resulting in over $19 billion for the Foundation School Fund and about $215 million for the Texas Veterans Commission over that time. Without this funding, the state would need other sources of revenue to make up for the over $2 billion the lottery brought in for education and veterans' programs last year. Although bingo attendance has been on the decline, the game is still an important source of revenue for Texas charities, which received about $32 million in bingo proceeds in fiscal year 2023. Bingo is also a source of funding for the state and for local governments. In fiscal year 2023, the state received nearly $16 million, and local governments received almost $13 million in bingo proceeds. No substantial benefit would result from transferring TLC's functions or merging them with another agency. Even though the review identified significant concerns with TLC's regulation of bingo, the agency provides the best available location for bingo regulation.

Key Recommendation

- Continue the Texas Lottery Commission for 12 years and remove the Sunset date of the agency's statutes.

Fiscal Implication Summary

Overall, the recommendations in this report would result in a loss to general revenue of about $68,000 per year.

Issue 2 — Modifying TLC's budget pattern to create a new goal for indirect administration would result in a gain to the Foundation School Fund. TLC would adjust fees to recover the amount currently subsidized by lottery funds, which would result in a gain to general revenue to pay for bingo's central administrative costs and deposits of an equal amount in the Foundation School Fund. Developing a plan to better prioritize updating CBOD's BOSS database and the Bingo Service Portal would have no fiscal impact. While implementing the plan would result in short-term IT costs, in the long term,

relying on more modern systems and eliminating paper-based processes would reduce administrative burdens and result in cost savings for the agency and licensees. Other recommendations would not result in any fiscal impact to the state.

Issue 3 — Eliminating manufacturer and distributor licenses would result in a loss of approximately $68,000 per year. While addressing grandfathered lessor licenses may have a fiscal impact on the industry, it cannot be estimated at this time.

Issue 4 — Continuing the Texas Lottery Commission for twelve years would require an annual appropriation from the Legislature, which was approximately $330 million per year for the 2024-25 biennium.

Texas Lottery Commission

Fiscal Year	Loss to the General Revenue Fund
2026	$68,000
2027	$68,000
2028	$68,000
2029	$68,000
2030	$68,000

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