

# Sunset Advisory Commission



**Texas Lottery  
Commission**

Staff Report  
April 2004

**TEXAS LOTTERY COMMISSION**

**SUNSET STAFF REPORT  
APRIL 2004**

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# **Table of Contents**

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	<b>PAGE</b>
<b>SUMMARY</b> .....	1
<b>STATUS OF 2002 SUNSET COMMISSION RECOMMENDATIONS</b> .....	5
<b>ISSUES / RECOMMENDATIONS</b>	
1 Texas Has a Continuing Need for the Texas Lottery Commission .....	11
2 The Small Size of the Texas Lottery Commission Limits Its Effectiveness and Communication Among Its Members .....	15
3 The Lottery Commission’s Analysis and Approval of Major Financial Decisions Could Be Strengthened .....	19
4 The Bingo Advisory Committee Has Progressed, but Needs Continued Improvement to Effectively Advise the Commission on Bingo Regulation in Texas .....	23
5 State Oversight of System Service Providers Is No Longer Needed .....	27
6 Key Elements of the State Lottery Act and the Bingo Enabling Act Do Not Conform to Commonly Applied Licensing Practices .....	31
<b>ACROSS-THE-BOARD RECOMMENDATIONS</b> .....	39
<b>AGENCY INFORMATION</b> .....	41

## **APPENDICES**

Appendix A — Equal Employment Opportunity Statistics .....	55
Appendix B — Historically Underutilized Businesses Statistics .....	59

# SUMMARY

## *Texas Lottery Commission*

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In 1980, Texas voters approved a constitutional amendment allowing the regulation of bingo for charitable fund-raising purposes. Voters approved another amendment in 1991 creating the state lottery to generate revenue for Texas government, and in 1997, the Legislature dedicated lottery revenue to public schools. To administer the lottery, the Legislature created the Texas Lottery Commission, and transferred bingo regulation to the new agency. Today, the Commission operates and markets the state lottery and regulates the charitable bingo industry through licensing and enforcement.

The Lottery Commission underwent Sunset review in 2002, and the Sunset Commission forwarded 24 recommendations to improve the agency to the Legislature in 2003. However, the Sunset legislation did not pass during the legislative session. Instead, the Legislature continued the Lottery Commission for two years and required a follow-up Sunset review to focus on the appropriateness of the Sunset Commission's 2002 recommendations. The results of that special purpose review are contained in this report. Overall, Sunset staff found that the Lottery Commission continues to effectively operate the lottery and regulate bingo, and therefore should be continued for 12 years.

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*The Lottery  
Commission continues  
to effectively operate  
the lottery and  
regulate bingo, and  
should be continued.*

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While the agency's Sunset legislation did not pass, the Lottery Commission has made a significant effort to address the issues raised in the 2002 staff report by implementing many of the Sunset Commission's recommendations without statutory direction. Despite the agency's actions, the current staff review found that some statutory changes are still necessary to ensure the agency continues to follow the Sunset recommendations in the future. In addition, the agency could not implement several of the recommendations without statutory authorization. The agency's progress in implementing the individual statutory recommendations is noted in the chart, *Status of 2002 Sunset Commission Recommendations*, on page 5.

Three of the Sunset Commission's 2002 statutory recommendations, concerning charitable distributions of bingo revenue and bingo lessor licensing, are not included in this report. During the 78th Regular Session, the Legislature passed House Bill 2519, which made many changes to the State's system of bingo regulation. To judge the effectiveness of these changes on the bingo industry, the agency needs time to implement them and bingo licensees need time to adjust to them. As a result, the Sunset Commission's 2002 recommendations related to the structure of bingo regulation are not recommended at this time.

One staff recommendation that the Sunset Commission did not adopt in 2002 is included in this report. The recommendation to abolish the regulation of system service providers was not addressed by the Sunset Commission

due to litigation regarding the license group that was pending at the time. Sunset staff raises the issue again in this report because the litigation has been resolved and the recommendation is still valid.

In addition to the Sunset Commission's recommended statutory changes, it also made a series of recommendations for management action. The Lottery Commission did not need statutory authorization for these changes and therefore was still required to comply with them during the past two years. As a result, Sunset staff does not recommend the same management actions again in this report. The chart, *Status At a Glance*, summarizes the agency's status in complying with the management actions. A more detailed discussion is provided in the chart, *Status of 2002 Sunset Commission Recommendations*.

<b>Status At a Glance 2002 Sunset Management Actions</b>	
Implemented	6
Partially Implemented	4
Not Implemented	2
<b>Total</b>	<b>12</b>

A summary of the recommendations in this report is provided in the following material.

## **Issues / Recommendations**

### **Issue 1**

***Texas Has a Continuing Need for the Texas Lottery Commission.***

#### **Key Recommendation**

- Continue the Texas Lottery Commission for 12 years.

### **Issue 2**

***The Small Size of the Texas Lottery Commission Limits Its Effectiveness and Communication Among Its Members.***

#### **Key Recommendation**

- Expand the Texas Lottery Commission from three to five public members.

### **Issue 3**

***The Lottery Commission's Analysis and Approval of Major Financial Decisions Could Be Strengthened.***

#### **Key Recommendations**

- Require the Commission to review and approve all major expenditures.
- Require the agency to develop a comprehensive business plan.
- The agency should use its cost-benefit analyses as a benchmark to judge the ongoing effectiveness of its expenditures.

## Issue 4

### ***The Bingo Advisory Committee Has Progressed, but Needs Continued Improvement to Effectively Advise the Commission on Bingo Regulation in Texas.***

#### **Key Recommendations**

- Require the Bingo Advisory Committee to develop an annual work plan and make recommendations to the Commission that identify specific issues that need addressing.
- Eliminate the statutory designation of a slot for a system service provider on the advisory committee.

## Issue 5

### ***State Oversight of System Service Providers Is No Longer Needed.***

#### **Key Recommendation**

- Abolish regulation of system service providers.

## Issue 6

### ***Key Elements of the State Lottery Act and the Bingo Enabling Act Do Not Conform to Commonly Applied Licensing Practices.***

#### **Key Recommendations**

- Ensure consistent licensing in the Bingo Enabling Act by providing clear licensure qualifications, eliminating requirements that unreasonably restrict licensure, providing a standard renewal process, and requiring the agency to review compliance history before license renewal.
- Standardize enforcement provisions in the State Lottery Act and the Bingo Enabling Act to provide for effective public protection and licensee compliance.

## **Fiscal Implication Summary**

This report contains recommendations that will have a fiscal impact to the State. These recommendations are discussed below.

- *Issue 2* – Expanding the Commission would result in additional travel expenses for two new members. The agency should use its administrative allocation of lottery revenue to pay the estimated \$3,200 per year in travel expenses for the new Commission members.
- *Issue 3* – Requiring the agency to develop a comprehensive business plan and requiring the Commission to review and approve all major expenditures could have a positive fiscal impact to the State by better ensuring all costs are reasonable and necessary. However, the amount of potential savings could not be estimated.
- *Issue 6* – Allowing the Commission to temporarily suspend a bingo license when tax revenue is at stake may result in fewer losses to the State. However, the number of suspensions is not known and the savings could not be estimated.



**STATUS OF 2002  
SUNSET COMMISSION RECOMMENDATIONS**

# Status of Recommendations

<b>Status of 2002 Sunset Commission Recommendations on the Texas Lottery Commission</b>	
<b>2002 Recommendation</b>	<b>Status</b>
<b>Issue 1 – Texas Has a Continuing Need for the Texas Lottery Commission.</b>	
<b>Change in Statute</b>	
1.1 Continue the Commission for 12 years.	Not Implemented – This recommendation requires a change in statute, as discussed in Issue 1 of this report.
<b>Issue 2 – The Small Size of the Texas Lottery Commission Limits Its Effectiveness and Communication Among Its Members.</b>	
<b>Change in Statute</b>	
2.1 Expand the size of the Commission from three to five public members.	Not Implemented – This recommendation requires a change in statute, as discussed in Issue 2 of this report.
<b>Issue 3 – The Lottery Commission Is Not Performing Sufficient Analyses to Guide Major Financial Decisions.</b>	
<b>Change in Statute</b>	
3.1 Require the Commission to review and approve all major expenditures.	Not Implemented – This recommendation requires a change in statute, as discussed in Issue 3 of this report.
3.2 Require the agency to develop a comprehensive business plan.	Partially Implemented – The agency recently entered into a contract to receive assistance in the development of its comprehensive business plan. The plan should be completed by July 2004, and the agency intends to update it annually thereafter. The agency would still benefit from having statutory language requiring the business plan to ensure that future agency administrators maintain the plan and continue to use it as a strategic planning tool, as discussed in Issue 3 of this report.
<b>Management Action</b>	
3.3 The agency should conduct a thorough cost-benefit analysis before approving new programs and expenditures.	Implemented – In 2003, the agency adopted an internal procedure establishing guidelines for preparing cost-benefit analyses. Since the procedure went into effect, the agency has produced more than 20 analyses.
3.4 The agency should evaluate the effectiveness of current program expenditures through program-specific performance measures or periodic justification reviews.	Partially Implemented – The agency says it reviews and evaluates performance measures for all of its programs during the biennial strategic planning process. This type of review is standard to all state agencies, but the agency could do more, as discussed in Issue 3 of this report.

**Status of 2002 Sunset Commission Recommendations on the  
Texas Lottery Commission**

2002 Recommendation	Status
<b>Issue 4 – Charities Are Not Making Maximum Charitable Distributions of Bingo Profits.</b>	
<b>Change in Statute</b>	
4.1 Require charities to distribute all bingo proceeds remaining after prizes and authorized expenses have been paid.	Statutory Alternative Implemented – The 78th Legislature passed HB 2519, which made many changes to the State’s system of bingo regulation. Both the agency and bingo licensees need time to adjust to those changes, and so the 2002 Sunset recommendations regarding charitable distributions are not included in this report.
4.2 Authorize the Lottery Commission to take enforcement action against charities that do not make a charitable distribution.	Statutory Alternative Implemented – The 78th Legislature passed HB 2519, which made many changes to the State’s system of bingo regulation. Both the agency and bingo licensees need time to adjust to those changes, and so the 2002 Sunset recommendations regarding charitable distributions are not included in this report.
<b>Management Action</b>	
4.3 The Commission should clarify the definition of charitable purpose and authorized expenses.	Partially Implemented – HB 2519 revised the statutory definition of charitable purposes to include any activity consistent with an organization’s federal tax exemption or with an organization’s charitable purpose. The bill also redefined authorized expenses to include any expense necessary to conduct bingo. The agency is currently developing rules to implement these statutory changes.
4.4 The Commission should work with the Legislative Budget Board to set performance measures for charitable distributions from bingo.	Implemented – The agency, along with the Legislative Budget Board, has developed two key outcome measures relating to the distribution of charitable bingo proceeds: 1) net bingo games revenue received by charitable organizations and 2) percent of organizations who fail to meet the 35 percent charitable distribution requirement.
<b>Issue 5 – Current Law Requires the Commission to Regulate Two Different Bingo Lessor License Systems.</b>	
<b>Change in Statute</b>	
5.1 Abolish the tiered lessor license structure and allow all commercial lessors to lease to up to seven charities.	Statutory Alternative Implemented – The 78th Legislature passed HB 2519, which made many changes to the State’s system of bingo regulation. Both the agency and bingo licensees need time to adjust to those changes, and so the 2002 Sunset recommendation regarding lessor licensing is not included in this report.

**Status of 2002 Sunset Commission Recommendations on the  
Texas Lottery Commission**

2002 Recommendation	Status
<b>Issue 6 – The Bingo Division Has Not Adequately Structured and Applied Its Enforcement Process.</b>	
<b>Change in Statute</b>	
6.1 Require the Lottery Commission to adopt rules governing all compliance monitoring and enforcement procedures.	Partially Implemented – The Lottery Commission has adopted rules that address bingo audit procedures, including a requirement that corrective measures for audit violations be completed in 30 days. The Commission is developing three more rules regarding audit procedures, as well as a rule establishing an administrative penalty matrix. The Commission’s responsibility to pass these and further rules would be reinforced by a statutory recommendation, as discussed in Issue 6 of this report.
6.2 Expand the Lottery Commission’s authority to temporarily suspend bingo licenses to prevent financial losses to the State.	Not Implemented – This recommendation requires a change in statute, as discussed in Issue 6 of this report.
<b>Management Action</b>	
6.3 The Lottery Commission should better coordinate the tracking of enforcement information.	Partially Implemented – The Commission is in the process of developing a comprehensive complaint system, called the Compliance Activity Monitoring System (CAMP), to coordinate all agency enforcement actions across divisions. CAMP will handle complaints from the moment they are received until they are resolved and analyze the sources and types of complaints. The agency expects to make the system operational by the end of calendar year 2004.
6.4 The Bingo Division should consider using its existing temporary suspension power.	Not Implemented – The agency interprets the threshold that has to be met to use its temporary suspension authority very stringently. Consequently, the agency has not used its temporary suspension authority since no enforcement cases have met this standard.
<b>Issue 7 – The Bingo Advisory Committee Does Not Effectively Advise the Commission on the Needs of the Bingo Industry in Texas.</b>	
<b>Change in Statute</b>	
7.1 Require the Bingo Advisory Committee (BAC) to develop an annual work plan and make recommendations to the Commission that identify specific issues that need addressing.	Implemented – The agency developed a work plan for BAC, including duties such as commenting on proposed rules and on the improvement and status of the bingo industry. However, the statutory recommendation is still appropriate to ensure that BAC continues to focus its activities in the future, as discussed in Issue 4 of this report.

**Status of 2002 Sunset Commission Recommendations on the  
Texas Lottery Commission**

<b>2002 Recommendation</b>	<b>Status</b>
7.2 Eliminate the statutory designation of a slot for a system service provider on BAC.	Not Implemented – The agency needs statutory authority to eliminate this slot, as discussed in Issue 4 of this report.
<b>Management Action</b>	
7.3 The Commission should evaluate the necessity of the Committee.	Implemented – The Commission recently evaluated and voted to continue BAC until August 31, 2005.
7.4 The Commission should ensure a greater balance between public and industry members on BAC.	Not Implemented – The Commission has not changed its rules regarding the composition of the advisory committee.
7.5 The Commission should lengthen Committee members' terms to three years and stagger the appointments.	Implemented – The Commission has changed its rules to provide for this recommendation. In February 2004, Committee members volunteered for the staggered terms.
7.6 The Commission should develop membership requirements for BAC.	Implemented – The Commission has adopted a rule to establish membership requirements for BAC.
7.7 The agency should assign an attorney to monitor BAC meetings.	Implemented – The agency assigned an attorney to attend BAC meetings and provide legal advice as needed.
<b>Issue 8 – Key Elements of the State Lottery Act Do Not Conform to Commonly Applied Licensing Practices.</b>	
<b>Change in Statute</b>	
8.1 Provide statutory language authorizing staggered license renewals.	No Longer Relevant – In the past, the agency had problems with high volumes of renewals at certain times of the year. This problem was mainly due to the large number of licenses the agency issued in the few months before it began selling lottery tickets in 1992. Over the years, monthly renewal volumes have become more consistent throughout the year and the agency states that peaks in renewals are no longer a problem.
8.2 Provide statutory language requiring the agency to review compliance history before renewing licenses.	No Longer Relevant – The agency maintains close supervision of lottery retailers and is able to summarily suspend licenses, thus allowing quick and decisive action when a retailer violates agency rules or laws. As a result, enforcement actions are consistently resolved before a license is eligible for renewal. This recommendation would not provide additional benefit to the agency, retailers, or the public.

**Status of 2002 Sunset Commission Recommendations on the  
Texas Lottery Commission**

<b>2002 Recommendation</b>	<b>Status</b>
8.3 Require the agency to analyze sources and types of complaints to identify and address problem areas and trends.	Partially Implemented – The agency’s CAMP system will allow it to analyze the sources and types of complaints it receives. This recommendation is still valid to ensure the agency continues to effectively manage complaints in the future, as discussed in Issue 6 of this report.
8.4 Provide statutory language to ensure complaints are investigated in a reasonable amount of time.	Partially Implemented – CAMP will allow the agency to track the length of time complaints are open. The system will also alert supervisors of complaints that have been open for a certain period of time. This recommendation for statutory change is still necessary to ensure the agency continues to effectively manage complaints in the future, as discussed in Issue 6 of this report.
8.5 Require the agency to provide public notice of its standard complaint process.	Partially Implemented – CAMP will help the agency better communicate its complaint procedures to the public. This recommendation for statutory change is still necessary to ensure the agency continues to effectively manage complaints in the future. The newly revised language of across-the-board recommendation 9, as noted on page 39, effectively incorporates the requirements of this recommendation.

**Issue 9 – Key Elements of the Bingo Enabling Act Do Not Conform to Commonly Applied Licensing Practices.**

**Change in Statute**

9.1 Require the agency to adopt clear qualifications for bingo licensure.	Partially Implemented – In April 2003, the Commission passed rules describing qualifications for bingo licensure. However, a statutory change is still appropriate, as discussed in Issue 6 of this report.
9.2 Eliminate statutory requirements governing the length of time conductors must be in existence to be eligible for a license.	Not Implemented – This recommendation requires a change in statute, as discussed in Issue 6 of this report.
9.3 Subject temporary licenses to standard oversight.	Not Implemented – The Commission has not subjected one-time temporary licenses to standard oversight. Issue 6 of this report makes a management recommendation to increase temporary license oversight.

**Status of 2002 Sunset Commission Recommendations on the  
Texas Lottery Commission**

<b>2002 Recommendation</b>	<b>Status</b>
9.4 Require the agency to create a standard license renewal process.	Partially Implemented – By rule, the Commission adopted a standard license renewal process in April 2003. However, a statutory change is still appropriate, as discussed in Issue 6 of this report.
9.5 Require the agency to review compliance history before renewing licenses.	Not Implemented – This recommendation requires a change in statute, as discussed in Issue 6 of this report.
9.6 Require the agency to adopt clear standards of conduct for licensees.	Not Implemented – The Commission has not adopted standards of conduct for bingo licensees. The recommendation requiring the agency to adopt such standards is still appropriate, as discussed in Issue 6 of this report.
9.7 Provide statutory language requiring the agency to maintain complaint information.	Implemented – The agency’s CAMP system will maintain all complaint information. The recommendation for statutory change is still necessary to ensure the agency continues to effectively manage complaints in the future. The newly revised language of across-the-board recommendation 9, as noted on page 39, effectively incorporates the requirements of this recommendation.
9.8 Provide statutory language to ensure complaints are investigated in a reasonable amount of time.	Partially Implemented – The agency’s CAMP system will allow the agency to track the length of time a complaint is open. The recommendation for statutory change is still needed to ensure the agency continues to effectively monitor complaints in the future, as discussed in Issue 6 of this report.
<b>Issue 10 – Certain Accounting Requirements for Bingo Conductors May Cause Inefficiency.</b>	
<b>Management Action</b>	
10.1 The Lottery Commission should study the concept of unit accounting.	Partially Implemented – HB 2519, as passed by the 78th Legislature, added language to the Bingo Enabling Act authorizing unit accounting. The agency is currently in the process of developing rules to implement the bill.

# ISSUES

## *Texas Has a Continuing Need for the Texas Lottery Commission.*

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### **Summary**

#### **Key Recommendation**

- Continue the Texas Lottery Commission for 12 years.

#### **Key Finding**

- No significant changes have occurred to affect the Sunset Commission's 2002 recommendation to continue the agency.

#### **Conclusion**

Texas has a continuing need to ensure the effective administration and operation of the lottery and regulation of bingo. These games constitute gambling and require close supervision by the State. The games also are an important source of revenue for the State, local jurisdictions, and local charities, and the Lottery Commission is responsible for maximizing lottery revenue and ensuring bingo revenue is spent on authorized purposes. In 2002, the Sunset Commission recommended that the Legislature continue the agency for 12 years. Sunset staff assessed the current appropriateness of the recommendation and concluded that the agency has generally been successful in accomplishing its mission and should be continued.

## Support

### **The Lottery Commission's mission is to administer the lottery and regulate bingo.**

- The mission of the Lottery Commission is to administer and market the lottery to generate revenue for the State and regulate bingo for charitable purposes. The agency is also responsible for maintaining the security and fairness of the lottery and bingo. The agency accomplishes these goals through the key functions of licensing, revenue collection, contract monitoring, marketing, and enforcement. The agency contracts with the GTECH Corporation to provide goods and services to the Lottery Commission in connection with the day-to-day operation of the lottery.
- In 1991, Texas voters approved a constitutional amendment to create the lottery as a means to generate revenue for the State. Until 1997, lottery revenues were deposited in the General Revenue Fund and were used to fund all manner of state expenditures. Since 1997, the Commission has deposited lottery revenues in the Foundation School Fund, which supports the operation and maintenance of public schools. Since 1999, unclaimed prize money has been deposited in accounts supporting indigent medical care. To administer the lottery, the Legislature may appropriate to the agency up to 7 percent of the gross revenue from the sale of lottery products. For the past five years, the agency has used less than 7 percent and returned the remainder to the Foundation School Fund.
- In 1980, voters approved a constitutional amendment allowing the State to regulate bingo and allowing voters to decide if they want bingo in their local jurisdictions. Approximately 200 local jurisdictions authorize bingo and nearly 1,400 charities are licensed to conduct bingo. Charities use their bingo revenue to support their charitable purposes. The Lottery Commission collects prize fees, rental taxes, and license fees on bingo and remits this revenue to the General Revenue Fund and a percentage of the prize fees to local jurisdictions that authorize bingo.

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*Lottery revenue contributes to the operation and maintenance of public schools.*

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*To date, the lottery has contributed more than \$11 billion to the State.*

### **No significant changes have occurred to affect the Sunset Commission's 2002 recommendation to continue the agency.**

- In 2002, the Sunset Commission recommended that the Legislature continue the Lottery Commission for 12 years. The recommendation is still appropriate. The lottery remains a consistent revenue generator for public schools and indigent health care, contributing approximately more than \$11 billion to the State since it was created. Since 1982, bingo has generated more than \$743 million for charitable purposes and \$472 million for the State and local jurisdictions. Without the revenue from these games, the State, charities, and local jurisdictions would have to find other funding sources.
- The Commission also continues to effectively operate the lottery and regulate bingo. While the agency outsources much of the operation of the lottery, it maintains the vital functions of ensuring the lottery is operated in accordance with state law. The agency actively markets the

lottery and its security staff investigates complaints from the public and tests games to ensure the accuracy of odds. Perhaps most importantly, the agency collects revenue from lottery retailers and remits it to the State Treasury.

The agency closely supervises bingo to see that the large sums of cash generated by charities conducting bingo are used for authorized purposes. To do this, the agency licenses bingo entities, reviews quarterly reports submitted by licensees, audits at-risk licensees, investigates complaints, and takes enforcement action against violators. The agency also collects revenue owed to the State from prize fees and rental taxes on bingo operations.

- During the 2002 review, Sunset staff considered several different organizational options for the agency. These other options included merging the Lottery Commission with the Racing Commission to form a new gaming commission, transferring the operation of the lottery back to the Comptroller's Office, allowing the agency to operate more independently from state government, and separating out the regulation of bingo. While all of these options still exist, the agency continues to function effectively, and staff concluded that the State would see no significant operational or administrative efficiencies from restructuring.

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*The agency effectively  
regulates the  
charitable bingo  
industry.*

## **Recommendation**

### **Change in Statute**

#### **1.1 Continue the Texas Lottery Commission for 12 years.**

This recommendation would continue the Texas Lottery Commission as the agency responsible for administering and marketing the State lottery and regulating charitable bingo.

### **Impact**

The intent of this recommendation is to continue the agency responsible for effectively administering the lottery to maximize revenue to the State and for regulating bingo to ensure bingo revenue is used for authorized purposes. The State has a continuing interest in ensuring the fairness and security of both the lottery and bingo. The State also has an interest in generating revenue for public schools and indigent health care, and in ensuring charities get the most benefit from the bingo games they conduct. The Lottery Commission has proven that it can accomplish these missions and should be continued for 12 years.

### **Fiscal Implication**

If the Legislature continues the current functions of the Lottery Commission, using the existing organizational structure, the agency's annual appropriation of approximately \$179 million would continue to be required for its operation. This appropriation is entirely paid for by the sale of lottery products and the licensing of bingo entities.



### *The Small Size of the Texas Lottery Commission Limits Its Effectiveness and Communication Among Its Members.*

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#### **Summary**

##### **Key Recommendation**

- Expand the Texas Lottery Commission from three to five public members.

##### **Key Finding**

- No significant changes have occurred to affect the Sunset Commission's 2002 recommendation to increase the size of the Lottery Commission.

##### **Conclusion**

The work of the Texas Lottery Commission in operating the lottery and regulating charitable bingo is hampered by its small size. As a three-member, part-time policy body, members of the Commission cannot informally discuss the work of the agency without violating the Open Meetings Act. The Commission also cannot form subcommittees to help it oversee the agency. In 2002, the Sunset Commission recommended that the Legislature increase the size of the Commission to five public members. Sunset staff assessed the current appropriateness of the recommendation and concluded that more members would allow the Commission to operate more effectively.

## Support

### **The Texas Lottery Commission is a three-member, part-time governing body.**

- In 1993, the Legislature created the Lottery Commission as a three-member body appointed by the Governor.
- The Commission usually meets once a month and is composed of public members, one of whom must have experience in the bingo industry. The Commission passes rules and sets policies to administer and operate the lottery and regulate bingo and employs the Executive Director, Charitable Bingo Operations Division Director, and Internal Auditor. The Commission also has authority to revoke and suspend lottery and bingo licenses and to deny bingo licenses after a hearing.

### **No significant changes have occurred to affect the Sunset Commission's 2002 recommendation to increase the size of the Lottery Commission.**

- In 2002, the Sunset Commission recommended to the Legislature that the size of the Lottery Commission be increased from three to five public members. That recommendation is still appropriate because the Commission's small size limits its effectiveness and internal communications. While the current Commissioners take great interest and are very involved in the agency's business, future Commissioners may not participate in the same way.
- While the Texas Open Meetings Act is intended to ensure policymaking bodies deliberate and make decisions in public, it can present difficult communication challenges for three-member boards. Because a meeting occurs any time a quorum discusses public business, three-member boards can violate the Act if two members ever discuss the agency's work without advance posting. As a result, two members of the Lottery Commission cannot directly talk with each other to informally discuss the work of the agency or share ideas. In fact, one member cannot even call another member to ask a question about basic Lottery Commission business.
- The small size of the Commission limits its use of subcommittees as a tool in overseeing the agency. While the Commission could create two-member subcommittees, it cannot have two subcommittees simultaneously working on different issues — a primary benefit of subcommittees. The current size of the Commission also limits the benefit of using subcommittees to divide the Commission's workload. Although Commission members may individually discuss matters with agency personnel, this option does not provide the difference of opinions that would come from having a subcommittee of members.
- The small size of the Commission also results in members relying heavily on agency staff for policy development. Individual Commissioners may not have the time to focus on a policy area, such as bingo regulation or procurement practices. Although bingo regulation is a small part of the agency's budget, it could benefit from greater oversight by the



*Commission members cannot informally discuss the work of the agency unless in a posted public meeting.*

Commission. A more financially significant function of the agency is managing numerous contracts for the operation of the lottery. The agency's nine largest contracts accounted for \$142 million, or 80 percent of the agency's lottery expenditures, in fiscal year 2003. The significant size of these contracts alone demands a high level of oversight by the Commission.

- The Legislature has generally created larger state agency governing bodies to properly carry out agency policymaking and oversight. Of 98 boards or commissions appointed by the Governor, only eight consist of three members, and three of those eight have members who serve full-time.<sup>1</sup>

## **Recommendation**

### **Change in Statute**

#### **2.1 Expand the Texas Lottery Commission from three to five public members.**

This recommendation would increase the size of the Lottery Commission by two members. Commissioners would continue to serve on a part-time basis and one member would still be required to have experience in the bingo industry. The Commission would still be subject to the Open Meetings Act when a quorum of its members deliberate and make decisions concerning the agency. However, with an expanded Commission, two members would be able to have informal discussions and share ideas concerning the agency. Further, with more members, the Commission should consider creating subcommittees to oversee bingo regulation, procurement practices, and any other functional areas needing a high level of oversight.

### **Impact**

Expanding the size of the Lottery Commission would increase the members' ability to communicate informally without violating the Open Meetings Act, allow the use of subcommittees, and allow individual members to focus more attention on significant functions of the agency. The recommendation does not intend that members of the Commission use their ability to meet informally as a method to circumvent the Open Meetings Act. The Commission would still have to comply with the Act.

### **Fiscal Implication**

This recommendation would have a minor fiscal impact to the State. Expanding the Commission would result in additional travel expenses for two new Commission members. Based on current projections, costs would increase by about \$1,600 per Commissioner per year. The agency currently receives up to 7 percent of lottery sales for its administration and should use this allocation to pay the travel expenses of the two new Commission members.

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<sup>1</sup> The Texas Commission on Environmental Quality, Public Utility Commission, and Workforce Commission are full-time commissions with three members each. The part-time, three-member boards or commissions with gubernatorial appointments are the Alcoholic Beverage Commission, Lottery Commission, Public Safety Commission, Transportation Commission, and Veteran's Land Board.



*The Lottery Commission's Analysis and Approval of Major Financial Decisions Could Be Strengthened.*

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## **Summary**

### **Key Recommendations**

- Require the Commission to review and approve all major expenditures.
- Require the agency to develop a comprehensive business plan.
- The agency should use its cost-benefit analyses as a benchmark to judge the ongoing effectiveness of its expenditures.

### **Key Findings**

- The agency has made a sincere effort to implement the 2002 Sunset Commission recommendations regarding its analysis of major financial decisions, but statutory changes are still needed.
- The agency should perform additional analysis of expenditures once they have been made.

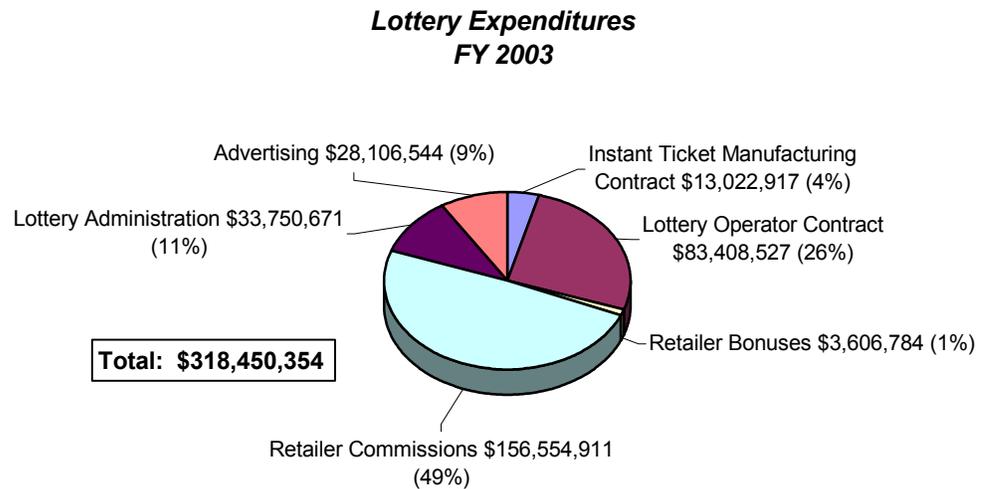
### **Conclusion**

The 2002 Sunset review evaluated the agency's analysis of major expenditures and found that several new expenditures were not thoroughly analyzed before approval, lacking cost-benefit comparisons and relying on insufficient or inaccurate data. Further, the State Lottery Act does not grant the Lottery Commission specific approval authority for contracts. In 2002, the Sunset Commission recommended that the Legislature require the Commission to approve all major expenditures and that the agency develop a business plan. Sunset staff assessed the current appropriateness of these recommendations and concluded that they are still necessary to help ensure the agency adequately evaluates and plans for its expenditures. The recommendations would also create a higher level of Commission oversight of major expenditures, in the interest of limiting administrative costs.

## Support

### The Texas Lottery Commission's appropriations and procurement structures are unlike other state agencies.

- The Legislature appropriates funding to the Lottery Commission based on up to 12 percent of the sales estimate for lottery products in the next year, as calculated by the Texas Comptroller of Public Accounts. Of this estimate, 5 percent goes to retailers for sales commissions, and the remaining 7 percent is used to cover the agency's administrative costs. The administrative allocations are shown in the pie chart, *Lottery Expenditures*. A contingency rider provides the agency with additional funding for contractual obligations if sales exceed budgeted amounts. The agency must return any unused administrative funds to the Foundation School Fund.



  
*The State Lottery Act vests all procurement authority with the Executive Director.*

- The State Lottery Act specifically exempts the Texas Lottery, but not the Charitable Bingo Operations Division, from the Texas Building and Procurement Commission's purchasing requirements and vests all procurement authority with the Executive Director. As a result, the Executive Director solely approves all major expenditures and procurement decisions. In fiscal year 2003, the Lottery Commission's nine major contracts accounted for more than \$142 million, or 80 percent of the agency's administrative expenditures. State law designates the Commission as the appellate body when a bidder protests a solicitation or contract award made by the Executive Director.

### The agency has made a sincere effort to implement the 2002 Sunset Commission recommendations regarding its analysis of major financial decisions, but statutory changes are still needed.

- In 2002, the Sunset Commission made a series of recommendations to the Legislature regarding the Lottery Commission's decisionmaking processes on major expenditures. During the 2002 review, Sunset staff found that the Commission was not sufficiently involved in major financial decisions and the agency had no business plan to provide a comprehensive strategy for its spending. Sunset staff found several

instances in which the agency made large expenditures without conducting complete, accurate cost-benefit analyses. The agency also did not perform sufficient post-expenditure analyses to ensure programs remained necessary and cost-effective. The report indicated that this lack of evaluation and planning could potentially lead to excessive spending, duplicative efforts, or ineffective programs.

To address these findings, the Sunset Commission recommended that the Lottery Commission, rather than the Executive Director, review and approve all major expenditures, and that the agency develop a comprehensive business plan. As direction to the agency's management, the Sunset Commission suggested it thoroughly evaluate new and existing programs and expenditures to ensure their effectiveness.

- In the past two years, the agency has done much to implement the Sunset Commission's recommendations. The Lottery Commission recently entered into a contract to receive assistance in the development of its comprehensive business plan. The plan will include all of the major components recommended by the Sunset Commission in 2002. The plan should be completed by July 2004, and the agency will update it annually thereafter. Although the agency has taken steps to implement this recommendation, it would still benefit from having statutory language requiring the business plan. Such language would ensure that future agency administrators maintain the business plan and continue to use it as a strategic planning tool. The recommendation requiring the Commission, rather than the Executive Director, to approve major expenditures is also still valid. The agency cannot implement this recommendation without statutory authority.

In 2003, the agency adopted an internal procedure establishing guidelines for preparing cost-benefit analyses. According to the procedure, each agency division must prepare a cost-benefit analysis whenever it is considering acquiring goods or services or renewing an existing contract worth more than \$25,000. Since the procedure went into effect, the agency has produced more than 20 analyses. As a result, the agency has successfully implemented this management recommendation and statutory change is not required.

**The agency should perform additional analysis of expenditures once they have been made.**

- One of the 2002 Sunset management recommendations directed the agency to periodically review current programs to evaluate the cost-effectiveness and necessity of those programs. In response, the agency says it reviews and evaluates performance measures for all of its programs during the biennial strategic planning process. In addition to that standard review, the agency now has an opportunity to do more in-depth analyses of existing programs as a result of its use of cost-benefit comparisons. These comparisons, done before expenditure decisions are made, can act as a benchmark for the agency to judge the performance of a program against the original expectations for that program. Such evaluations can help the agency further ensure the effectiveness and efficiency of its expenditures.



*The 2002 Sunset recommendations are still needed to ensure the agency continues analyzing and planning for major expenditures.*

## Recommendations

### Change in Statute

#### **3.1 Require the Commission to review and approve all major expenditures.**

This recommendation would give procurement authority to the Commission, which could delegate certain procurement duties to the Executive Director. This authority is typical for most state boards and commissions. All major procurements would require Commission review and approval. The Commission would determine, by rule, which procurements would be considered major, based on the cumulative value of the contract, as well as other relevant factors.

#### **3.2 Require the agency to develop a comprehensive business plan.**

The Lottery Commission's major initiatives should be guided by a comprehensive business plan to ensure their cost effectiveness. The business plan should include a specific description of each program, key management information, accurate financial data, and a detailed financial management plan. The Commission should review the business plan at least annually to assess the overall performance and value of each project. Projects that fail to meet financial objectives should be adjusted or terminated. This recommendation will build on recent efforts by the agency and ensure that business planning continues in the future.

### Management Action

#### **3.3 The agency should use its cost-benefit analyses as a benchmark to judge the ongoing effectiveness of its expenditures.**

Since the agency has begun performing cost-benefit analyses of major expenditures, it should use this information to determine whether those expenditures are achieving their original objectives once underway. Further, by comparing a program's original expectations to its ongoing performance, the agency will be able to judge the accuracy of the projections provided in its cost-benefit analyses.

### Impact

These recommendations would promote more effective oversight of Lottery Commission expenditures. Requiring a comprehensive business plan will ensure analysis of major projects and procurements to see that their costs and benefits are clearly and accurately identified before approval, and that the program is clearly in line with the business direction of the agency. In addition, greater Commission involvement will increase accountability and result in more informed policy decisions.

### Fiscal Implication

These recommendations could potentially have a positive fiscal impact to the State. Oversight of major programs and procurements should ensure that the actual costs of agency initiatives, as well as a reasonable estimate of the benefit of the initiative, are taken into consideration when committing public funds, potentially reducing the administrative costs of the agency. Costs in preparing the agency-wide business plan should be offset by resulting savings, and any savings resulting from lower administrative costs would provide additional funding to the Foundation School Fund.

### *The Bingo Advisory Committee Has Progressed, but Needs Continued Improvement to Effectively Advise the Commission on Bingo Regulation in Texas.*

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#### **Summary**

##### **Key Recommendations**

- Require the Bingo Advisory Committee to develop an annual work plan and make recommendations to the Commission that identify specific issues that need addressing.
- Eliminate the statutory designation of a slot for a system service provider on the advisory committee.

##### **Key Finding**

- The Lottery Commission has implemented most of the 2002 Sunset Commission recommendations aimed at improving the Committee, but some statutory changes are still needed.

##### **Conclusion**

The purpose of the Bingo Advisory Committee is to advise the Lottery Commission on the needs and problems of the charitable bingo industry. The 2002 Sunset review found that the Committee was ineffective at providing the Commission with useful feedback, and that its membership structure limited its ability to focus on significant issues. Consequently, the Sunset Commission made several recommendations to improve the Committee's effectiveness and ability to serve as a useful resource to the Commission. Though the Commission has implemented many of these recommendations, it still needs statutory authority to effect all the changes envisioned by the last Sunset review.

## Support

### The Bingo Advisory Committee advises the Texas Lottery Commission on charitable bingo issues.

<b>BAC Appointments</b>	
1	General Public
3	Conductors (charities operating bingo games)
1	Lessor, Charity
2	Lessors, Commercial
1	Distributor or Manufacturer
1	System Service Provider

- The Bingo Advisory Committee (BAC) consists of nine members, appointed by the Commission, representing a variety of interests, as shown in the textbox, *BAC Appointments*. BAC meets quarterly or at the Commission's request and must adhere to the Open Meetings Act as required by agency rule. Members are not reimbursed for expenses. The responsibilities of the Committee are to:
  - advise the Commission on the needs and problems of the state's bingo industry;
  - comment on bingo rules during their development and before final adoption unless an emergency requires immediate action by the Commission;
  - report annually to the Commission on the Committee's activities; and
  - perform other duties as determined by the Commission.

### The Lottery Commission has implemented most of the 2002 Sunset Commission recommendations aimed at improving the Committee, but some statutory changes are still needed.

- In 2002, the Sunset review found that the Bingo Advisory Committee did not effectively carry out its duties to advise the Lottery Commission, was disorganized, did not approach its duties with a clear focus, and did not present any tangible recommendations to the Commission. The review also found that the Committee's structure limited its effectiveness due to its members' short terms and constant turnover, its limited public membership, and its lack of membership requirements.
- As a result of these findings, the Sunset Commission made two statutory recommendations, including requiring the Bingo Advisory Committee to develop an annual work plan and eliminating the system service provider slot on the Committee. The Sunset Commission also made a series of management recommendations including directing the Lottery Commission to evaluate the Committee's necessity, ensure a greater balance of public members, lengthen members' terms and stagger appointments, and develop membership requirements. The Sunset Commission also directed the agency to assign an attorney to monitor all BAC meetings.
- Over the past two years, the Lottery Commission has implemented most of the Sunset recommendations. The Commission approved a work plan for BAC and recently evaluated the Committee, voting to continue it until August 31, 2005. The Commission developed committee membership requirements and changed members' terms to staggered three year terms. The Commission also assigned an attorney to monitor committee meetings and provide legal guidance when necessary. More information on the implementation of Sunset's 2002



*In 2002, the Sunset review found that BAC did not effectively carry out its duties.*

recommendations can be found in the chart, *Status of 2002 Sunset Commission Recommendations*, on page 5 of this report.

- Though agency staff developed a work plan in 2003 for BAC, the statutory recommendation to require the Committee itself, not agency staff, to develop a work plan annually is still appropriate. Requiring the Committee to annually update the work plan would ensure that the Committee continues to focus its activities on issues designed to assist the Commission in its regulation of bingo. Requiring the Commission to approve the work plan would encourage continued communication between BAC and the Commission and would give the Commission opportunity to provide direction to the Committee. In addition, following an approved plan would assist the Committee to focus on its mission and avoid time spent discussing issues aimed at improving the financial outlook of the bingo industry. Such discussions are best left for the industry itself and not for an advisory committee created to focus on regulatory issues.
- In 2002, the Sunset Commission recommended eliminating the system service provider (SSP) slot on BAC. This recommendation is still appropriate since the slot is statutorily assigned and SSPs represent a minuscule fraction of the regulated community. Issue 5 of this report recommends abolishment of the SSP licensing program.



*Requiring BAC to develop an annual work plan would help it to focus its activities on bingo regulation.*

## Recommendations

### Change in Statute

#### **4.1 Require the Bingo Advisory Committee to develop an annual work plan and make recommendations to the Commission that identify specific issues that need addressing.**

This recommendation requires the Committee to develop a yearly work plan that would detail its objectives and issues it would like to address during the year. This work plan should be formally approved by the Lottery Commission in a public meeting. The issues addressed by BAC should include assessing how trends in the charitable bingo industry relate to Commission regulation, reviewing bingo rules for needed changes, additions, or deletions, and addressing other issues as determined by the Commission. At year's end, BAC should assess its accomplishments, identify opportunities to improve the way the agency regulates charitable bingo, and develop specific recommendations for Commission action.

#### **4.2 Eliminate the statutory designation of a slot for a system service provider on the advisory committee.**

Since the agency only licenses one system service provider, this recommendation would eliminate an unnecessary slot on the Bingo Advisory Committee. The Commission could fill this position with a person representing the general public or another license group.

## **Impact**

The intent of the recommendations is to improve the effectiveness of BAC in meeting the needs of the Commission and its regulation of the bingo industry. The recommendation to develop an annual work plan would provide the Committee with focus and direction on the issues it addresses each year. The recommendation would also increase the usefulness of the information BAC provides to the Commission.

## **Fiscal Implication**

These recommendations would not result in a fiscal impact to the State.

## *State Oversight of System Service Providers Is No Longer Needed.*

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### **Summary**

#### **Key Recommendation**

- Abolish regulation of system service providers.

#### **Key Finding**

- Regulating system service providers continues to offer little benefit to the State or the public and limits the availability of automated accounting services to conductors.

#### **Conclusion**

The Commission licenses system service providers (SSPs), who provide tracking and accounting programs to bingo conductors. Since SSP licensure began in 1995, the Commission has licensed only four SSPs. Currently, the Commission regulates only one SSP and no conductor uses the services of the licensed provider. The 2002 Sunset review evaluated the need for continuing this licensing program by using the Texas Sunset Act criteria, such as identification of the objectives including the problem or need for the function and the extent to which those objectives have been achieved. Sunset staff found that these objectives have not been realized and the regulation is not needed. Due to pending litigation at the time, the Sunset Commission did not address this recommendation in 2002, however, the litigation has since been resolved, and the staff recommendation warrants reconsideration.

## Support

### **The Lottery Commission regulates system service providers.**

- In 1995, the Legislature gave the Commission the power to regulate system service providers (SSPs) through licensure. In theory, SSPs supply automated bingo services to licensed conductors, which are charities that conduct bingo games. As defined by state law, automated bingo services are computer programs that register and account for bingo sales, prizes, inventory, and prize fees; generate reports for the Commission; and provide bingo conductors with other information for accounting and business purposes. By rule, automated bingo services do not include computer accounting programs that are commercially available, such as Quickbooks.

State law requires SSPs to have their automated bingo services system approved by the Commission prior to supplying or selling it to a conductor, to file quarterly reports with the Commission, and to pay an annual \$1,000 licensing fee.

### **Regulating system service providers continues to offer little benefit to the State or the public and limits the availability of accounting services to conductors.**

- In 2002, the Sunset Commission took no action on the regulation of SSPs due to ongoing litigation at that time. However, that District Court case relating to the definition of automated bingo services has been dismissed and the licensed SSP pursuing the litigation surrendered his license to the Commission. Currently, only one SSP is licensed by the Commission. Consequently, Sunset staff feels that this recommendation is still appropriate since the licensure program continues to be little used, offers no benefit to the public, and wastes agency resources.
- The Commission licenses SSPs to ensure that conductors using automated bingo services receive a legitimate product, licensed within the scope of the Bingo Enabling Act. However, the Commission only licenses one SSP and has not approved that licensee's automated bingo system. As a result, no conductor uses the services of a system service provider.
- The 2002 staff report also noted that state law prohibits any other bingo licensee from also being licensed as an SSP or providing automated bingo services. For example, licensed bingo equipment manufacturers and distributors cannot provide any type of accounting or equipment-tracking system for bingo conductors, though they provide other types of automated products. The Commission states that some manufacturers could provide some of these services, if not limited by the current statute.
- Although no conductor uses these automated bingo services, the Commission expends time and money regulating them. The agency estimates it spent a cumulative 278 hours regulating SSPs in the last 18 months. This includes time spent by legal, security, bingo licensing, and bingo auditing staff at the Commission.

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*The Lottery Commission only licenses one SSP, and has not approved that licensee's automated bingo system.*

## **Recommendation**

### **Change in Statute**

#### **5.1 Abolish regulation of system service providers.**

This recommendation would abolish the licensing requirements for system service providers and the regulation of automated bingo services. Any licensee choosing to use such services in the future will continue to be subject to all provisions of the Act and agency rule. If licensing were repealed, the section of the Bingo Enabling Act that requires one member of the current nine-member advisory committee to be a system service provider should also be repealed, as provided for in Issue 4 of this report.

### **Impact**

Eliminating the regulation of system service providers seeks to lessen unnecessary state regulation. Since no conductor uses these services, the program has never fulfilled the Legislature's expectations for providing bingo conductors with regulated accounting programs and is not needed. Abolishing regulation will allow other entities to provide conductors with accounting products and services that state law currently considers automated bingo services. As required by current law, conductors will remain accountable for the accuracy of records submitted to the Commission.

### **Fiscal Implication**

This recommendation would not result in a fiscal impact to the State. Savings from eliminating licensure of the existing SSP would be offset by reductions in licensing revenue, or \$1,000 per year, per license.



## *Key Elements of the State Lottery Act and the Bingo Enabling Act Do Not Conform to Commonly Applied Licensing Practices.*

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### **Summary**

#### **Key Recommendations**

- Ensure consistent licensing in the Bingo Enabling Act by providing clear licensure qualifications, eliminating requirements that unreasonably restrict licensure, providing a standard renewal process, and requiring the agency to review compliance history before license renewal.
- Standardize enforcement provisions in the State Lottery Act and the Bingo Enabling Act to provide for effective public protection and licensee compliance.

#### **Key Findings**

- The Lottery Commission has taken steps to implement many of the 2002 Sunset Commission recommendations, but still needs statutory authority for many of the needed changes.
- Licensing provisions in the Bingo Enabling Act do not follow model licensing practices, affecting the fair treatment of licensees and limiting public protection.
- Nonstandard enforcement provisions of the State Lottery Act and the Bingo Enabling Act potentially reduce the agency's effectiveness regarding public protection and the safeguarding of state revenue.

#### **Conclusion**

Various processes in the State Lottery Act and the Bingo Enabling Act do not match model licensing standards developed by Sunset staff from experience gained through more than 80 occupational licensing reviews over the last 25 years. In 2002, the Sunset review compared the Lottery Commission's statutes, rules, and practices to the model licensing standards to identify variations. Based on these variations, the Sunset Commission recommended changes needed to bring the regulation in line with model standards. Though the Lottery Commission has taken steps to implement many of the 2002 Sunset Commission recommendations, it still needs statutory authority for many changes.

## Support

**Regulating activities that require licensure, such as the lottery and bingo, requires common functions that the Sunset Commission has observed and documented over more than 25 years of reviews.**

- The Texas Lottery Commission regulates both the lottery and bingo and performs several standard licensing and enforcement functions. To be eligible to sell lottery tickets in Texas, individuals and entities must complete and submit an application to the Lottery Commission. The agency currently regulates about 16,300 licensed lottery retailers. The agency's enforcement methods include summary suspension and license revocation or suspension after a hearing for lottery licenses.

The agency's Charitable Bingo Operations Division licenses all bingo-related activities and monitors the distribution of charitable proceeds. The Bingo Division currently regulates 1,389 conductors, 449 commercial lessors, 15 distributors, 15 licensed manufacturers, and one system service provider. The agency's various enforcement methods for bingo licenses include license suspension and revocation after a hearing, administrative penalties, and injunctive relief.

- The Sunset Advisory Commission has a historic role in evaluating licensing agencies, as the increase of occupational licensing programs served as an impetus behind the creation of the Commission in 1977. Since then, the Sunset Commission has completed more than 80 licensing agency reviews. Sunset staff has documented standards in reviewing licensing programs to guide future reviews of licensing agencies. While these standards provide a guide for evaluating a licensing program's structure, they are not intended for blanket application.

**The Lottery Commission has taken steps to implement many of the 2002 Sunset Commission recommendations, but still needs statutory authority for many of the needed changes.**

- The Lottery Commission has implemented many of the licensing and enforcement recommendations the Sunset Commission approved in 2002, as shown in the chart, *Status of 2002 Sunset Commission Recommendations*, on page 5. For example, the Commission has passed several rules outlining bingo enforcement procedures and the agency has embarked on an ambitious effort to create a universal complaint tracking system that will coordinate all agency enforcement actions across divisions.

However, the agency continues to lack statutory authority to make some changes, and, in some cases, the agency should still have statutory direction to ensure it continues complying with the recommendations in the future. The following material highlights areas where the agencies' statutes and rules continue to differ from model standards, and describes the potential benefits of bringing the statutes and rules into conformity with standard practices.



*Since 2002, the Lottery Commission has embarked on an ambitious effort to create a complaint tracking system.*

**Licensing provisions in the Bingo Enabling Act do not follow model licensing practices, affecting the fair treatment of licensees and limiting public protection.**

- ***Qualifications for licensure.*** The statutes or policies of licensing agencies should not require qualifications for licensure that cannot be determined concretely or that have little or no bearing on protecting the public. Although the Bingo Enabling Act describes the license application, it does not list specific qualifications for issuance of a license, such as competency or character prerequisites. Easily determined, clear qualifications would provide both the licensee and the public notice of general licensing requirements.
- ***Restricting practice.*** Care should be taken to ensure that licensing provisions do not unnecessarily limit entry to the business. To be eligible for a bingo conductor's license, the current statute requires an organization to be in existence a minimum amount of time to ensure the validity of the organization. For example, to obtain a license to conduct bingo, religious societies are required to exist in Texas for at least eight years, historical associations for five years, and fraternal organizations for three years. An internal policy only requires volunteer fire departments to exist for one year. Different lengths of existence arbitrarily limit licensing of certain organizations without a sound basis for licensee or public protection.
- ***Standard renewal process.*** A licensing agency should have a renewal process that incorporates ways to ensure continued competence of licensees before renewing a license. While the statute provides specific guidelines for bingo conductor license renewal, no renewal provisions exist in statute for bingo lessors, manufacturers, distributors, or system service providers. Without specific provisions, licensees are not aware of standard renewal guidelines.
- ***Compliance history.*** Before renewing a license, a licensing agency should be aware of any compliance issues that a licensee might have and the licensee's efforts to resolve those problems. Existing enforcement actions should be in the process of resolution or fully addressed before an agency renews a license. Tracking an applicant's history of compliance with administrative actions will assist in enforcement and ensure that all enforcement actions are resolved before licensure.
- ***Temporary licenses.*** In general, a temporary license authorizes the holder to practice without meeting all licensure qualifications. Such a license should be authorized only in very limited circumstances since the public is offered no assurance of competency, and charitable revenue may not be protected. The Bingo Enabling Act currently authorizes temporary bingo licenses for special occasions, totaling about 2,800 in calendar year 2002. About 20 percent of these temporary licenses are not subject to the same level of oversight as other licenses, and are never inspected or audited.



*Different lengths of  
existence required for  
bingo licensure  
arbitrarily limit  
licensing of  
organizations.*

**Nonstandard enforcement provisions in the State Lottery Act and the Bingo Enabling Act could reduce the agency's effectiveness in providing fair treatment to licensees, protecting consumers, and safeguarding state revenue.**

**Lottery and Bingo**

- *Analyzing complaints.* Analysis of complaint information is a useful way to identify regulatory problem areas. Sources of complaints could include the general public, the licensee population, other agencies or institutions, or the licensing agency itself. Types of complaints could cover a wide range of topics, such as qualifications for licensure, compliance with established rules, and quality of service. In 2002, the Sunset review found that the Lottery Commission maintained a complaint database, but did not perform any further analysis of complaints.
- *Investigation time.* Investigations that are unreasonably long can prolong potentially dangerous situations for the public or disrupt licensee activities. Although some investigations require more time than others, the agency should monitor time elapsed to keep investigations within reasonable time boundaries. Currently, only internal procedures suggest that investigations should be completed in a reasonable amount of time.

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*In 2002, the Sunset review found that the Lottery Commission did not sufficiently analyze complaints.*

**Bingo**

- *Standards of conduct.* Standards of conduct define appropriate behavior for licensees. These standards give the public a guide for judging appropriate behavior and a basis for complaining to the agency when these standards are not met. Standards of operation or definitions of how certain tasks should be accomplished are also helpful to the affected public to determine whether a function was performed appropriately. These standards are most useful in situations where licensees have close contact with the public, or where their behavior could cause serious financial implications.

The Bingo Enabling Act authorizes the Commission to deny a renewal for any cause that would permit or require suspension or revocation. The language authorizing suspension or revocation is similar, citing any reason that would allow or require the Commission to refuse to issue or renew a license of the same class. This circular statutory language leaves only one broad requirement for denials, renewals, revocations, and suspensions: the licensee must comply with the Act and Commission rules. Currently, no rules or policies list specific qualifications for licensure, or even certain situations for denying licensure. No specific standards of conduct are available to notify the licensee or provide the agency a sound basis for acting on certain complaints.

- *Full range of penalties.* An agency should have authority for a full range of penalties to ensure that appropriate sanctions for offenses are available to it. The full range of penalties include revocation of a license, suspension of a license, refusal to renew a license, probation of a suspended license, and reprimand. Currently, the Bingo Division does not have authority to probate a suspended license, depriving the agency of a useful enforcement tool.

- **Compliance monitoring.** An agency should have clear procedures, rules, and statutory authority for conducting inspections that help ensure standard treatment of licensees and timely resolution of violations. In 2002, the Sunset review found that the Bingo Division's compliance and enforcement processes were not defined in rule.
- **Schedule of Sanctions.** Agencies that impose sanctions for violations of law or rule should use a schedule of sanctions to establish appropriate actions for specific violations. The schedule helps ensure fair and consistent treatment of all violators, and should be adopted by the agency's policymaking body so that the public has an opportunity for comment. The 2002 Sunset review found that the Lottery Commission lacked rules to provide guidance in assessing administrative penalties against bingo licensees, which limits the agency's ability to ensure consistent application of those penalties.
- **Temporary Suspension.** Consideration should be given to granting an agency suspension power if the agency regulates activities that can result in substantial and immediate harm to the public. The Commission currently has authority to temporarily suspend bingo licenses if a licensee's continued operation may constitute an immediate threat to the health, safety, morals, or welfare of the public. However, under its current authority, the agency is unable to suspend a license to prevent financial loss to the State if a licensee fails to remit the required quarterly taxes or prize fees. As a result, the agency is unable to prevent organizations from continuing to incur liability against the State.

  
*The agency's current temporary suspension authority does not allow suspension of a bingo license for failure to remit quarterly taxes.*

## Recommendations

### Licensing

#### Change in Statute

##### **6.1 Require the agency to adopt clear qualifications for bingo licensure.**

This recommendation would require the agency to develop, through rule, comprehensive licensing qualifications. By listing specific qualifications for licensure, licensees and the public are provided sufficient notice of licensing requirements. Guidelines would also assist the agency in consistent licensing, and provide a sound basis for license denials and other enforcement matters.

##### **6.2 Eliminate statutory requirements governing the length of time bingo conductors must be in existence to be eligible for a license.**

This recommendation would eliminate varying existence requirements for conductors currently in statute. Instead, the statute would require the Commission to adopt rules establishing standard time periods for the existence of all types of conductors. This change would ensure organizations are legitimate and established, and eliminate inconsistent standards for different types of organizations.

##### **6.3 Require the agency to create a standard bingo license renewal process.**

This recommendation would require the Commission, through rule, to document its renewal process from submission to completion. The Commission would adopt provisions addressing license renewals for all licensees to ensure continued competency of the licensee. These guidelines will provide notice, maintain consistency, and designate standard renewal practices.

**6.4 Require the agency to consider compliance history before renewing bingo licenses and authorize denial of license renewals based on outstanding administrative sanctions.**

This recommendation would require the agency to consider compliance history before all license renewals, providing the agency statutory authority to deny renewals based on the licensee's outstanding noncompliance with an existing agency enforcement action. Considering compliance history before license renewals will ensure timely resolution of any compliance issues and also increase accountability.

## **Management Action**

**6.5 The agency should increase oversight of temporary bingo licenses where appropriate.**

The Lottery Commission should consider subjecting temporary licenses to the same oversight requirements provided in statute for standard licenses, where appropriate.

## **Enforcement**

### **Change in Statute**

**6.6 Require the agency to analyze sources and types of all complaints to identify and address problem areas and trends.**

This recommendation would require the agency to analyze its reported complaint activity to identify any trends or issues concerning certain violations. The agency could use this information to educate its licensees, focus on common problems, and possibly change regulatory language to address new concerns.

**6.7 Provide statutory language to ensure all complaints are investigated in a reasonable amount of time.**

This recommendation would help ensure speedy resolution of complaints by requiring investigations to be completed in a reasonable amount of time, which should be defined by the Commission in rule. Though a current internal policy encourages timely resolution, statutory language would formalize adherence to reasonable time requirements, and provide public notice of expected time frames for resolution.

**6.8 Require the agency to adopt clear standards of conduct for bingo licensees.**

This recommendation would require the Commission to adopt, by rule, standards of conduct developed by the agency. Comprehensive standards of conduct would include ethical standards and appropriate behavior for bingo licensees. This recommendation would give notice to both the public and licensees of appropriate standards of practice, and provide greater enforcement authority for the agency to act on various complaints. Adopting standards through the rulemaking process provides bingo licensees and the public an opportunity to participate in the development of these rules.

**6.9 Provide the Commission with authority to put suspended bingo licensees on probation.**

This recommendation would give the Commission a full range of administrative sanctions for its bingo licensees, allowing the agency to put a suspended licensee on probation. If the agency chooses to use probation as a sanction, it should have clear probation standards in rule, including procedures

for imposing appropriate conditions, notifying probationers of those conditions and actions they need to take, and tracking probationers' progress.

**6.10 Require the Commission to adopt rules governing all bingo compliance monitoring and enforcement procedures.**

This recommendation would require the Lottery Commission to develop rules that provide a framework for its compliance monitoring efforts, such as audits and inspections, and enforcement activities. The recommendation would also require the Commission to develop, by rule, timelines for resolutions of violations found in audits. A licensee would have to prove corrective measures or be subject to sanctions within the established timelines.

**6.11 Require the Commission to adopt a schedule of sanctions for bingo enforcement actions in rule.**

The recommendation would direct the agency to develop a penalty structure, by rule, to guide the application of administrative penalties against licensees for failing to comply with the statute and rules. Such a penalty structure would ensure the appropriate application of penalties to each violation. The Commission would develop a list to define or summarize the most common violations, and a schedule of penalties tied to the seriousness and frequency of particular offenses. The penalty structure would allow for deviations if mitigating circumstances are involved, for which the Commission would need to clearly establish reasons.

**6.12 Expand the Lottery Commission's authority to temporarily suspend bingo licenses to prevent financial losses to the State.**

This recommendation would amend the agency's existing temporary suspension authority to include the ability to temporarily suspend a bingo license in instances where action is necessary to prevent financial loss to the State. For example, the Bingo Division Director could issue a temporary suspension order if a licensee fails to remit quarterly taxes or prize fee payments to the agency. To implement this recommendation, the Commission would be required to adopt rules governing the use of its temporary suspension authority.

## **Impact**

The application of these recommendations to the State Lottery Act and the Bingo Enabling Act would result in efficiency and consistency from standardization, additional administrative flexibility, equitable processes for licensees, and additional protection of revenue and the public. The following chart, *Benefits of Recommendations*, categorizes the recommendations according to their benefits.

## **Fiscal Implication**

These recommendations would not have a significant fiscal impact to the State. The recommendations change procedures in ways that should not require additional resources. Allowing the Commission to temporarily suspend a bingo license when tax revenue is at stake may result in fewer losses to the State, however, the savings cannot be estimated.

<b>Benefits of Recommendations</b>				
<b>Recommendations</b>	<b>Efficiency of Operations</b>	<b>Administrative Flexibility</b>	<b>Fairness to Licensee</b>	<b>Public Protection</b>
<b>Licensing</b>				
6.1 Require the agency to adopt clear qualifications for bingo licensure.	✓		✓	✓
6.2 Eliminate statutory requirements governing the length of time bingo conductors must be in existence to be eligible for a license.	✓		✓	✓
6.3 Require the agency to create a standard bingo license renewal process.		✓	✓	✓
6.4 Require the agency to consider compliance history before renewing bingo licenses and authorize denial of license renewals based on outstanding administrative sanctions.	✓	✓		✓
6.5 The agency should increase oversight of temporary bingo licenses where appropriate.		✓	✓	✓
<b>Enforcement</b>				
6.6 Require the agency to analyze sources and types of all complaints to identify and address problem areas and trends.		✓	✓	✓
6.7 Provide statutory language to ensure all complaints are investigated in a reasonable amount of time.	✓		✓	✓
6.8 Require the agency to adopt clear standards of conduct for bingo licensees.	✓		✓	✓
6.9 Provide the Commission with authority to put suspended bingo licensees on probation.	✓		✓	✓
6.10 Require the Commission to adopt rules governing all bingo compliance monitoring and enforcement procedures.	✓		✓	✓
6.11 Require the Commission to adopt a schedule of sanctions for bingo enforcement actions in rule.	✓		✓	✓
6.12 Expand the Lottery Commission's authority to temporarily suspend bingo licenses to prevent financial losses to the State.	✓	✓		✓

## **ACROSS-THE-BOARD RECOMMENDATIONS**

**Texas Lottery Commission**

<b>Recommendations</b>	<b>Across-the-Board Provisions</b>
Already in Statute	1. Require public membership on the agency's policymaking body.
Update	2. Require provisions relating to conflicts of interest.
Update	3. Require unbiased appointments to the agency's policymaking body.
Already in Statute	4. Provide that the Governor designate the presiding officer of the policymaking body.
Update	5. Specify grounds for removal of a member of the policymaking body.
Apply	6. Require training for members of the policymaking body.
Apply	7. Require separation of policymaking and agency staff functions.
Apply	8. Provide for public testimony at meetings of the policymaking body.
Apply	9. Require information to be maintained on complaints.
Apply	10. Require the agency to use technology to increase public access.
Apply	11. Develop and use appropriate alternative rulemaking and dispute resolution procedures.



## **AGENCY INFORMATION**

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# Agency Information

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In 1991, Texas voters approved a constitutional amendment authorizing a state lottery. In 1993, the Legislature created the Texas Lottery Commission (the Commission) to assume the administration of the lottery and also transferred the administration of the Bingo Enabling Act to the new agency. Today, the Commission administers and markets the state lottery and regulates the charitable bingo industry through licensing and enforcement.

## Key Facts

- **Funding.** The Commission operated with a budget of \$193.7 million in fiscal year 2003 – all of which came from lottery proceeds and bingo licensing fees.
- **Lottery Revenue.** In fiscal year 2003, the lottery generated about \$3.1 billion in revenue, of which \$882 million was transferred to the Foundation School Fund. During that same year, the agency transferred unclaimed prize money totaling \$66.9 million to accounts benefitting indigent health care. The remainder of the proceeds pay for prizes, the agency's administrative costs, and retailer commissions. Through fiscal year 2003, the Texas Lottery transferred \$10.8 billion dollars to the State.
- **Bingo Revenue.** In calendar year 2003, charitable bingo generated \$573 million in revenue, of which \$30 million was distributed for charitable purposes. Also in that year, the Commission collected about \$24.9 million in prize fees, licensing fees, and rental taxes from the conduct of bingo.
- **Staffing.** The Commission has 325 full-time equivalent positions. Nearly three-quarters of the positions are located in the Austin headquarters and the rest are in the Commission's 16 claim centers and five regional offices.
- **Licensing.** The Commission regulates approximately 16,307 lottery retailers, 1,389 bingo conductors, 449 bingo lessors, 15 bingo equipment manufacturers, 15 bingo equipment distributors, and one bingo system service provider.
- **Enforcement.** In fiscal year 2003, the agency received 800 complaints for both lottery and bingo, resolved 772 complaints, inspected 727 licensed lottery retailers,



*On the Internet:  
Information about the lottery  
and bingo is available on the  
at [www.txlottery.org](http://www.txlottery.org) and  
[www.txbingo.org](http://www.txbingo.org).*

### Mission Statement

- The Texas Lottery is committed to generating revenue for the State of Texas through the responsible management and sale of entertaining lottery products. The Texas Lottery will incorporate the highest standards of security and integrity, set and achieve challenging goals, provide quality customer service and utilize a team approach.
- Provide authorized organizations the opportunity to raise funds for their charitable purposes by conducting bingo. Determine that all charitable bingo funds are used for a lawful purpose. Promote and maintain the integrity of the charitable bingo industry throughout Texas.

### Recipients of Lottery Revenue FY 2003

*Foundation School Fund* - Supports the operation and maintenance of public schools. School districts may use money from this fund for purposes such as purchasing supplies, library books, equipment and teacher salaries.

*Multicategorical Teaching Hospital Account* - Supports the reimbursement of indigent care at the University of Texas Medical Branch at Galveston.

*Tertiary Care Facility Account* - Supports State-designated trauma center hospitals in reimbursing the cost of indigent care.

and inspected and audited 1,045 bingo licensees and applicants. Additionally, the Commission issued 363 agency orders resulting in sanctions.

- **Contracts.** The Commission outsources many key lottery functions including lottery games operation. The contracted lottery operator, GTECH Corporation, is responsible for providing lottery information technology systems, equipment, and sales staffing. In fiscal year 2003, the Commission spent about \$83.4 million on this contract. The Commission's other major contracts include advertising services and instant ticket manufacturing.

## Major Events in Agency History

- 1980** Texas voters approve a constitutional amendment authorizing charitable bingo on a local option basis.
- 1982** The Bingo Division of the Comptroller of Public Accounts issues the first bingo licenses.
- 1990** The Legislature transfers regulation of charitable bingo to the Texas Alcoholic Beverage Commission.
- 1991** Texas voters approve a constitutional amendment to create a state lottery. The lottery is administered by the Lottery Division of the Comptroller of Public Accounts.
- 1992** The Lottery Division issues the first lottery retailer licenses and the sale of instant and online tickets begins.
- 1993** The Legislature creates the Texas Lottery Commission to administer the lottery and transfers regulation of charitable bingo to the new agency effective April 1, 1994.
- 1995** The Bingo Advisory Committee, created by the Legislature in 1993, holds its first meeting.
- 1997** The Legislature amends the State Lottery Act to direct all lottery proceeds to the Foundation School Fund, rather than the General Revenue Fund. The Legislature also amends the Bingo Enabling Act to require the Director of the Charitable Bingo Operations Division to report directly to the Lottery Commission, rather than to the Executive Director of the agency.
- 2003** The Legislature authorizes the Texas Lottery to join a multi-jurisdictional lottery game and the sale of tickets for *Mega Millions* begins.

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*In 2003, the Texas Lottery began selling tickets for Mega Millions, a multi-jurisdictional lottery game.*

## Organization

### Policy Body

The Commission is composed of three members appointed by the Governor with the advice and consent of the Senate to serve staggered six-year terms. One member must have experience in the bingo industry. The chart, *Texas*

*Lottery Commission Policy Body*, contains information on current members. To be appointed to the Commission, an individual must have been a Texas resident for at least ten consecutive years immediately before appointment.

<b>Texas Lottery Commission Policy Body</b>			
<b>Member</b>	<b>City</b>	<b>Qualification</b>	<b>Term Expiration</b>
C. Tom Clowe, Jr., Chair	Waco	Public Member, with experience in the bingo industry	2005
James A. Cox, Jr.	Austin	Public Member	2009
Rolando Olvera, Jr.	Brownsville	Public Member	2007

The Commission sets policies to administer and promote the lottery and regulate bingo. The Commission also has authority to revoke and suspend licenses issued under the State Lottery Act and the Bingo Enabling Act and to deny bingo licenses after a hearing. The Commission generally meets once a month in Austin.

The Commission receives assistance on bingo issues from the statutorily-authorized Bingo Advisory Committee. This Committee consists of nine members representing the public, charities that operate bingo games, commercial and charity lessors that participate in the bingo industry, distributors and manufacturers of bingo supplies, and one system service provider. The Commission appoints new members with recommendations from existing Committee members. The responsibilities of the Committee are to:

- advise the Commission on the needs and problems of the state’s bingo industry;
- comment on bingo rules during their development and before final adoption unless an emergency requires immediate action by the Commission;
- report annually to the Commission on the Committee’s activities; and
- perform other duties as determined by the Commission.

**Staff**

The agency is organized into two main areas – lottery and bingo. The Executive Director oversees the day-to-day activities of the lottery and administration of the agency. A separate Director oversees the Charitable Bingo Operations Division and reports directly to the Commission. The agency’s security, legal, human resources, information technology, and other administrative functions are shared by both the lottery and bingo sides of the organization. The chart, *Texas Lottery Commission Organizational Chart*, depicts the agency’s organization.

In fiscal year 2004, the agency has 325 full-time equivalent positions. Nearly three-quarters of the agency’s employees are located at the headquarters in Austin. A total of 90 employees are divided between the agency’s 16 claim

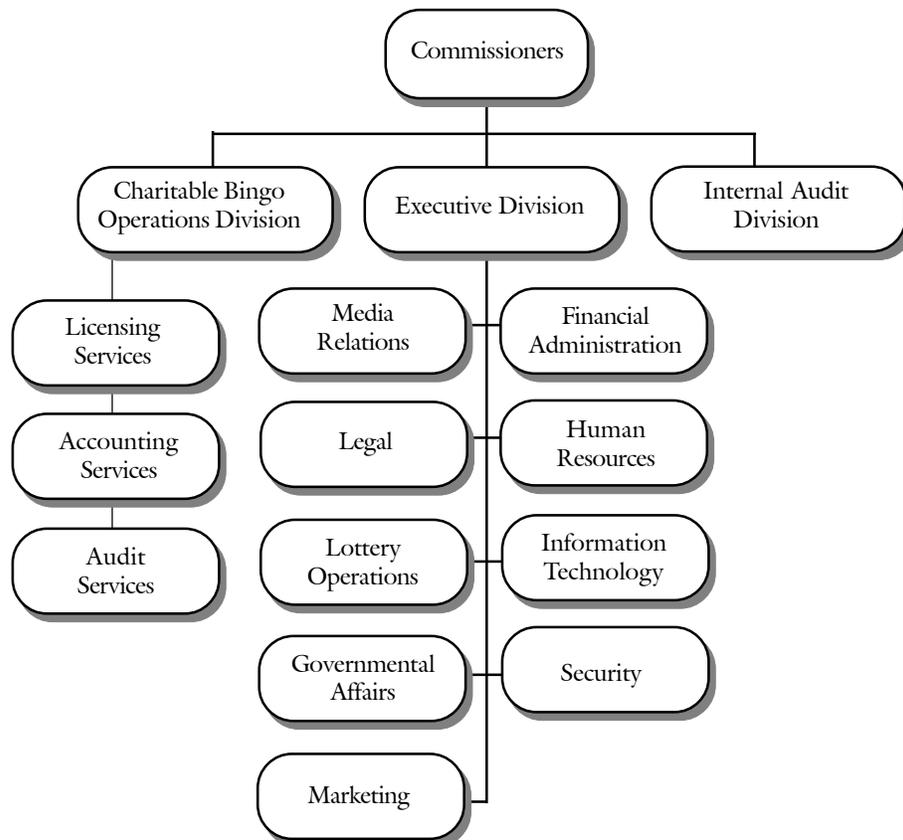
  
*The Lottery Commission sets policies to administer and promote the lottery and regulate bingo.*

centers located throughout the state and five regional bingo and security offices. The table, *Commission Employees by Office*, shows the distribution of employees at the agency's headquarters and satellite offices. The map, *Claim Centers and Regional Offices*, shows the location of these satellite offices.

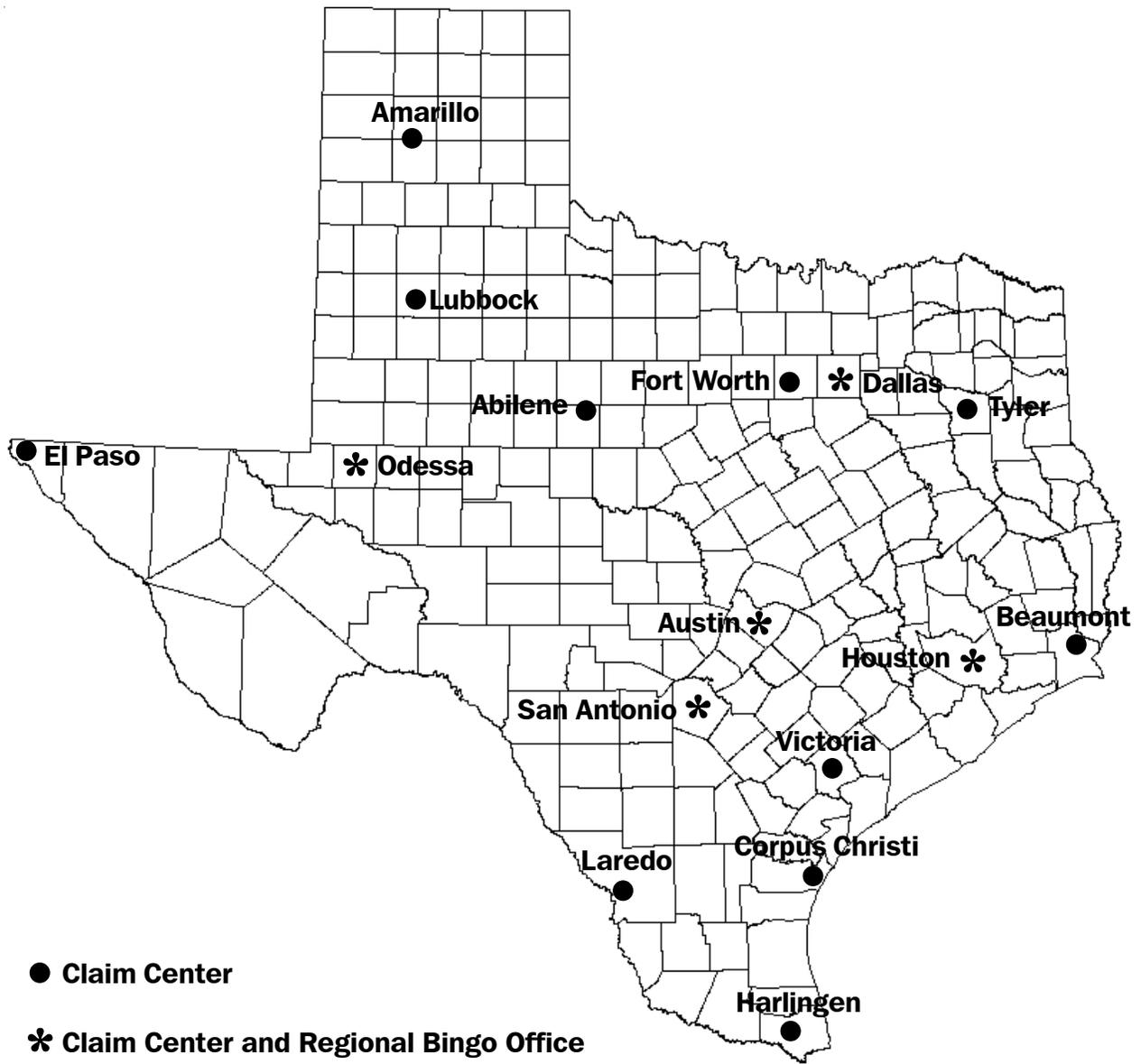
<b>Commission Employees by Office</b>		
<b>Office</b>	<b>Location</b>	<b>Number of Positions</b>
Headquarters	Austin	235
Claim Centers	16 locations throughout the state	49
Regional Bingo Offices	Austin, Dallas, Houston, Odessa, San Antonio	22
Regional Security Offices	Austin, Dallas, Houston, Odessa, San Antonio	19
Total Positions		325

A comparison of the agency's workforce composition to the minority civilian labor force over the past four years is shown in Appendix A, *Equal Employment Opportunity Statistics*. The Commission generally met or exceeded the statewide civilian labor force percentages for most job categories.

**Texas Lottery Commission  
Organizational Chart**



## Claim Centers and Regional Offices



# Funding

## Revenues

The Lottery Commission's appropriations for fiscal year 2003 totaled \$193.7 million for administration of the lottery and regulation of bingo. The agency received more than 98 percent of its revenues from the sale of lottery products. To administer the lottery, the statute entitles the Commission to up to 12 percent of the lottery proceeds, at least 5 percent of which is dedicated to lottery retailers in the form of commissions. Lottery proceeds and licensing fees are deposited into the General Revenue Lottery Dedicated Account and the agency receives its appropriation from this account. If the agency does not use its full appropriation, it must return that money to the Foundation School Fund. In fiscal year 2003, the agency returned \$7.8 million in unspent administrative funds.

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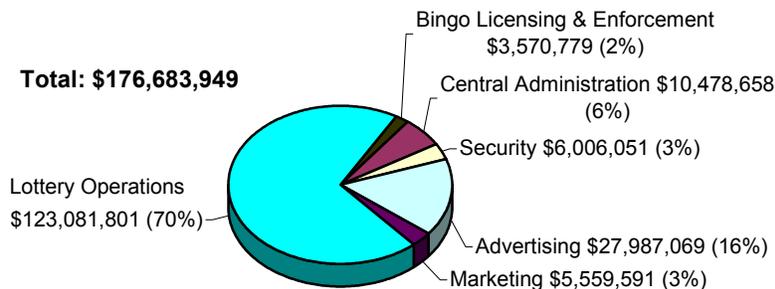
*In 2003, more than two-thirds of the agency's expenditures were for operation of the lottery.*

The Lottery Commission also generates revenue for the State from prize fees, rental taxes, and license fees on bingo operations. This money is paid into the General Revenue Fund and a portion of it is appropriated to the agency for the purpose of regulating bingo, accounting for less than 2 percent of the agency's budget. More detailed information about revenues from the sale of lottery products and bingo regulation is provided in the following agency operations section.

## Expenditures

In fiscal year 2003, more than two-thirds of the agency's expenditures were for the operation of the lottery, as shown in the pie chart, *Expenditures by Strategy*. The next largest portion of the agency's budget went toward marketing and advertising to promote lottery products. Other expenditures include security, administration, and bingo regulation.

**Expenditures by Strategy  
FY 2003**



Appendix B describes the Commission's use of Historically Underutilized Businesses (HUBs) in purchasing goods and services for fiscal years 2000 to 2003. In fiscal year 2003, the Commission spent nearly three-quarters of its budget on outside contractors, mainly for services such as lottery operations, instant

ticket manufacturing, and advertising. The Commission generally exceeded the statewide goals for professional services and commodities, but fell short of the goals for special trade and other services.

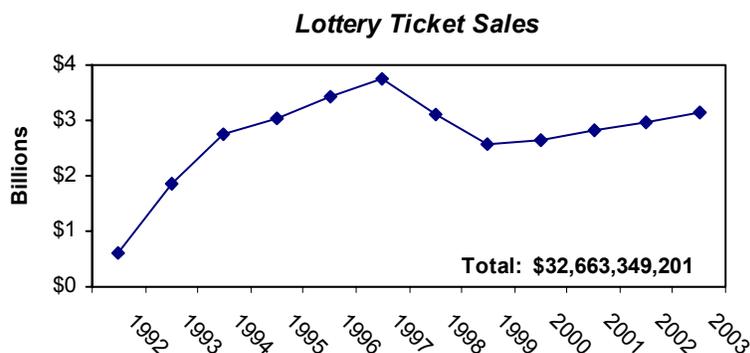
## Agency Operations

The mission of the Lottery Commission is to administer and market lottery games to generate revenue for the State and to regulate bingo to maximize charitable distributions. The agency is also responsible for maintaining the

security, fairness, and integrity of lottery games, and the fairness and integrity of bingo games. The agency accomplishes these goals through key functions such as overseeing the operation of the lottery, licensing lottery retailers and bingo industry representatives, collecting revenue generated through the sale of lottery products and the conduct of bingo games, marketing the lottery, ensuring compliance with lottery and bingo statutes and regulations, and taking enforcement action against violators.

## Lottery

In 1991, Texas voters approved a constitutional amendment to create a state lottery. Through fiscal year 2003, the lottery generated \$10.8 billion for the State's general revenue, public schools, and indigent care programs. As shown in the chart, *Lottery Ticket Sales*, the lottery remains a consistent revenue generator. Further, according to the agency's most recent demographic study, approximately 56 percent of all adult Texans have played at least one Texas Lottery game in the past year.



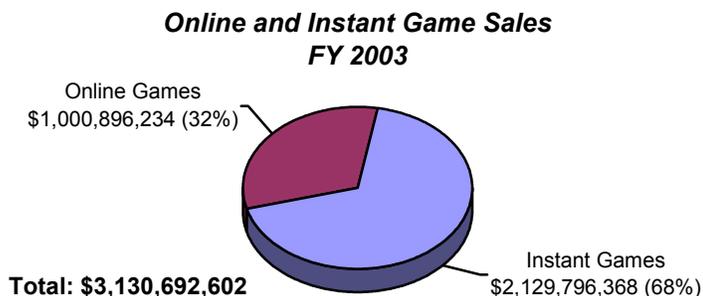
## Products and Revenues

The Commission has two different lottery products, online and instant games, which are sold by licensed lottery retailers. Online games are games in which players select a set of numbers, the type of game, and amount of play for a specified drawing date. The Commission administers the drawing of the winning numbers of each game on a set schedule. The Commission currently has five types of online games: *Lotto Texas*, *Pick 3*, *Cash Five*, *Texas Two Step*, and *Mega Millions*, the multi-state lottery game.

Instant games, also called scratch-off games, are games in which players buy a preprinted ticket with symbols hidden underneath a latex cover that correspond to prizes. Currently, the Commission has about 81 different scratch-off games ranging in price from \$1 to \$20. The pie chart, *Online and Instant Game Sales*, gives sales information about the Commission's games for fiscal year 2003.

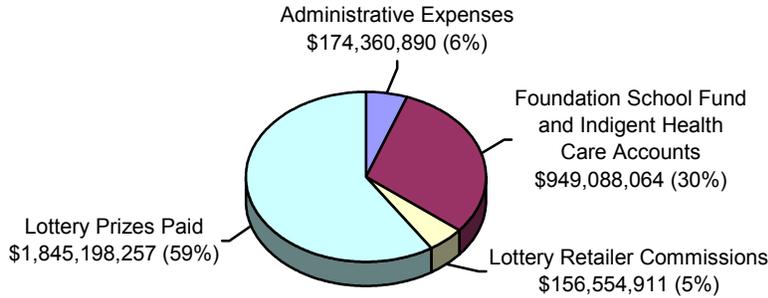
★

*Through fiscal year 2003, the lottery generated \$10.8 billion for the State.*



The pie chart, *Lottery Revenue Distributions*, shows how the money generated by the lottery was distributed in fiscal year 2003. Of the revenue generated each year, 12 percent is reserved to cover operating costs of the lottery,

**Lottery Revenue Distributions  
FY 2003**

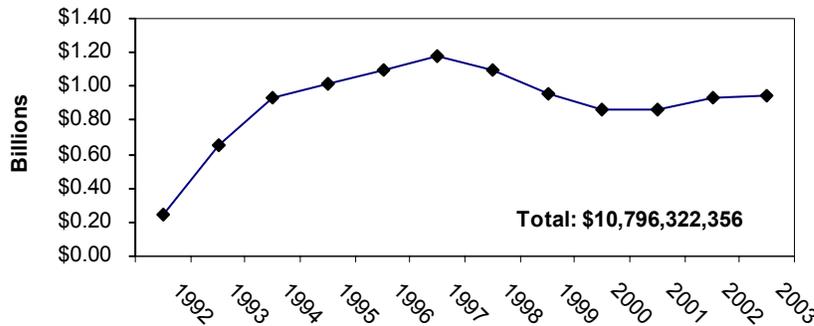


**Total: \$3,125,202,122**

with up to 7 percent covering the cost of the agency's administration and 5 percent returning to lottery retailers as sales commissions. Prize amounts for lottery tickets are also deducted from the total ticket sales. The remainder of the revenue collected is transferred to the State. The chart, *Revenue Transfers to the State*, shows trends in the amount of money transferred to the State since the lottery's inception through fiscal year 2003.

In 1997, the Legislature amended the State Lottery Act to direct lottery proceeds to the Foundation School Fund, rather than to the General Revenue Fund. Later, in 1999, the Legislature specified that the first \$40 million of any unclaimed prize money, which was previously returned to the prize pool, be directed to the Multicategorical Teaching Hospital Account, and any money in excess of that \$40 million per biennium will be transferred to the Tertiary Care Facility Account.

**Revenue Transfers to the State**



Beginning in fiscal year 2004, the first \$10 million of unclaimed prize money is deposited in the Multicategorical Teaching Hospital Account, and the remainder goes to the General Revenue Fund. The textbox, *Total Transfers to the State*, shows how much money the Commission has transferred to each of these funds from 1992 to 2003.

unclaimed prize money is deposited in the Multicategorical Teaching Hospital Account, and the remainder goes to the General Revenue Fund. The textbox, *Total Transfers to the State*, shows how much money the Commission has transferred to each of these funds from 1992 to 2003.

<b>Total Transfers to the State FY 1992 - 2003</b>	
General Revenue Fund 1992 - 1997	\$5,130,647,837
Foundation School Fund 1998 - 2003	\$5,454,606,636
Multicategorical Teaching Hospital Account 2000 - 2003	\$80,000,000
Tertiary Care Facility Account 2001 - 2003	\$131,067,883

## **Operations**

The Texas Lottery is the only lottery in the United States that outsources its entire lottery sales function. The Commission works closely with its contracted lottery operator, GTECH Corporation, to administer the lottery. The lottery operator's responsibilities under its contract with the Commission include:

- instant ticket and online gaming system design, operation, and maintenance;
- lottery management system design, operation, and maintenance;
- telecommunications network design, operation, and maintenance;
- marketing research, promotions, and field sales personnel and services;
- instant ticket and online ticket stock warehousing, packing, and distribution;
- ticket order processing and telemarketing; and
- hotline support system operation.

Under its contract with the Commission, the lottery operator must meet several guidelines set by the Commission and the Legislature, such as sales goals, average prize payout percentages, and ethical and security standards. The lottery operator provides goods and services in connection with the day-to-day operations of the lottery, but the Commission retains the right to make all decisions regarding the direction and control of the lottery. Though the lottery operator administers the Commission's instant ticket games functions, the Commission contracts with three instant ticket manufacturers to produce the tickets: Scientific Games International, Pollard Banknote Limited, and Oberthur Gaming Technologies.

## **Claim Centers**

The Lottery Commission operates 16 claim centers around the state to provide lottery information to players and redeem prizes. Players may redeem their winning tickets and collect prizes that are worth less than \$1 million at these claim centers. For prizes of \$1 million or more, winners must travel to Austin to claim their money. In addition, lottery retailers may redeem prizes of less than \$600. The agency's claim centers issue approximately 900 prize checks per week statewide. The claim centers also provide information about lottery games to the public through an average of 1,400 walk-in interactions and 2,600 calls to the agency's toll-free phone line per week. The agency's Austin staff encourages large jackpot winners to seek legal and financial advice before claiming the prize and will assist winners in how to deal with media inquiries.

## **Licensing**

To be eligible to sell lottery tickets in Texas, individuals and entities must complete and submit an application to the Lottery Commission. After criminal and financial background checks, the agency will issue a lottery retailer license. The agency will deny a license if an applicant's history includes felony convictions, misdemeanor convictions involving moral



*The Texas Lottery outsources its entire lottery sales function to its lottery operator, GTECH.*



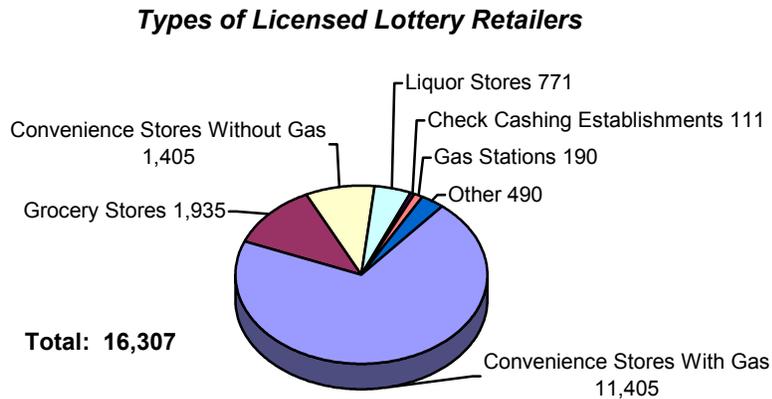
*The agency's claim centers issue about 900 prize checks per week.*

turpitude, convictions of gambling or gambling-related offenses, professional gambling, delinquent taxes, or personal or fiduciary relationships with the agency or lottery operator.

The agency processes all lottery retailer applications, license renewals, and terminations; updates retailer information; and coordinates ownership

transfers and lottery terminal moves.

Lottery retailer licenses are valid for two years. The agency's licensing staff handles about 1,200 transactions per month. The agency regulates approximately 16,307 licensed lottery retailers, of which 41 percent are chain stores and 59 percent are independent retailers. As shown in the chart, *Types of Licensed Lottery Retailers*, more than three-quarters of licensed retailers are convenience stores.



### Compliance and Enforcement

The Lottery Commission is responsible for vendor and retailer compliance and enforcement. The agency closely monitors the performance of its vendors to ensure they are in compliance with contract requirements. For example, the agency monitors the services provided by the lottery operator vendor such as instant ticket storage and delivery, field visits to retailers, ticket returns, and terminal installations. The agency also monitors its instant ticket vendors for quantity and quality control. If a vendor does not comply, the agency can assess penalties for not performing specific contracted services.

The agency also closely monitors lottery retailers for compliance with statutory licensing requirements. For example, the agency oversees the weekly electronic transfers, or sweeps, of lottery revenues from retailer bank accounts to the State Treasury and currently monitors approximately 204 delinquent accounts. If weekly sweeps find insufficient funds, the agency may take action against the retailer's license, such as summary suspension or revocation. If an issue is not resolved within a reasonable time, the agency can use collection tools such as freezing bank accounts or obtaining liens. The agency may also suspend a retailer license if the agency determines that the retailer location is non-compliant with the Americans with Disabilities Act requirements. Before proceeding to suspend or revoke a retailer's license, the agency can withhold any bonus incentive payments due to the retailer for selling certain prize-winning tickets. In fiscal year 2003, 1,515 summary suspensions were imposed, meaning some licenses were suspended on more than one occasion, and 353 licensing proceedings were held before the State Office of Administrative Hearings. During that same year, the agency revoked 119 licenses.

★  
*In fiscal year 2003, the agency imposed 1,515 summary suspensions of lottery retailer licenses.*

## Marketing and Advertising

The Lottery Commission provides planning, development, production, distribution, marketing, and promotion of online and instant ticket games to maximize the sale of lottery products. The agency contracts with two advertising firms to generate television, radio, print, and outdoor advertisements for both general and minority markets. Approximately 13,000 radio spots and 5,000 television commercials are aired monthly. These firms also help the agency coordinate statewide on-air promotions. The agency spent nearly \$28 million on these advertising contracts in fiscal year 2003. In addition, the agency planned, coordinated, and staffed 86 promotional events in fiscal year 2003. The agency also researches the demographics of lottery players. The textbox, *Who Plays the Lottery?*, shows some of the results of this research.

### Who Plays the Lottery?

According to the agency's most recent demographic study:

- 44 percent of lottery players have an annual income of \$50,000 and over;
- 67 percent have some college education; and
- 45 percent are 36 to 55 years old.

The demographic study also showed that the gender and ethnic makeup of lottery players roughly matches that of the state's population in general.

## Bingo

The Lottery Commission also regulates all activities related to conducting charitable bingo games in the state. Charitable bingo allows nonprofit organizations to raise funds for their charitable purposes. To ensure that charities conduct their bingo games fairly and use proceeds derived from bingo games for authorized purposes, the Commission performs core regulatory functions including licensing, inspecting, auditing, and enforcement. A 1980 constitutional amendment authorized bingo on local option basis and required that proceeds from bingo be spent in Texas for charitable purposes. Currently, approximately 200 local jurisdictions in Texas allow bingo. In calendar year 2003, 22.6 million people attended bingo games in Texas.

### Bingo Games

Bingo may be played using traditional paper cards, pull-tabs, and electronic card-minding devices. Pull-tabs are instant bingo tickets with perforated break open tabs that may conceal prize symbols. Electronic card-minding devices enable a player to play up to 66 bingo card faces at a time with one computerized device. The Lottery Commission tests and approves paper cards, pull-tabs, electronic card-minding devices, and pull-tab dispensers. Manufacturers submit new pull-tab games to the agency to test for accuracy of prize payouts and for quality and security of the games.

Most bingo games offer prizes. By law, the maximum prize per game is \$750 and the maximum prize per four-hour bingo session is \$2,500. In 2003, the prizes paid to bingo players totaled \$414.9 million.

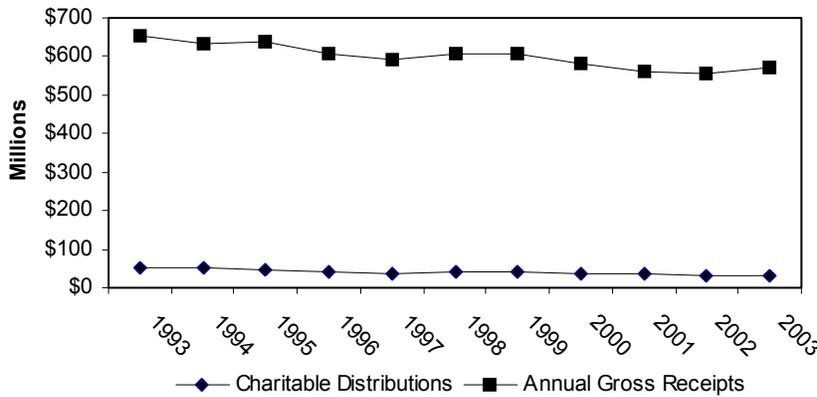
### Revenue

In calendar year 2003, charitable bingo games generated \$573 million in gross receipts. The graph, *Bingo Revenue and Charitable Distributions*, shows bingo revenue distributed for charitable purposes over the last ten years. Bingo generates revenue for a variety of charitable purposes such as helping veterans with their medical costs, providing scholarships to disadvantaged students, and supporting halfway houses that treat individuals with substance



*In calendar year  
2003, charitable  
bingo games  
generated \$573  
million in gross  
receipts.*

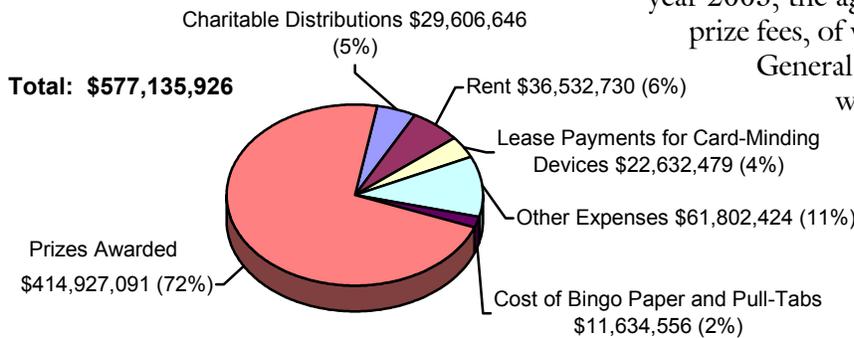
**Bingo Revenue and Charitable Distributions**



abuse problems. An organization licensed to conduct bingo must distribute a minimum of 35 percent of its adjusted gross receipts minus the licensee’s authorized expenses. Overall, these expenses reduce the charitable distribution to approximately 5 percent of total gross receipts. A breakdown of how bingo revenue was used in calendar year 2003 is illustrated in the pie chart, *Bingo Expenditures*.

In addition to revenue generated for charitable purposes, bingo also produces revenue for the State and for local jurisdictions through prize fees and taxes. The organizations conducting bingo collect 5 percent of all bingo prizes awarded, which they then remit to the agency. Most local jurisdictions choose to receive half of the prize fees generated by bingo in their area. In calendar year 2003, the agency collected \$20.6 million in prize fees, of which \$11.1 million went to the General Revenue Fund and \$9.7 million was returned to local jurisdictions. The agency also collects a tax imposed on the rental of premises where bingo is conducted. Persons leasing their premises for conducting bingo pay a 3 percent gross rental tax on the rental income they receive. In calendar year 2003, the agency collected \$1.1 million in gross rental taxes that went to the General Revenue Fund.

**Bingo Expenditures  
Calendar Year 2003**



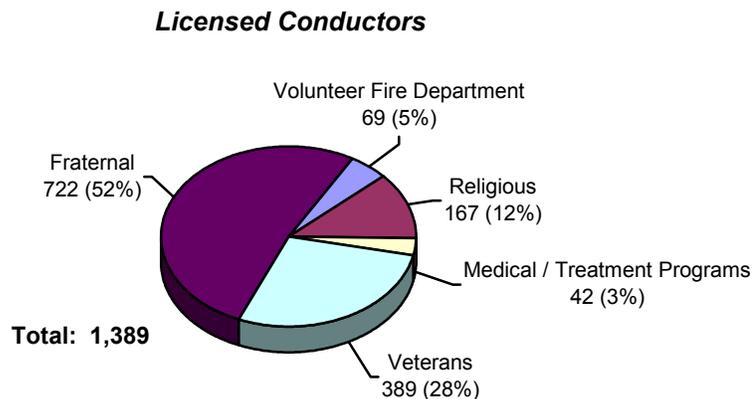
**Licensing**

The Lottery Commission licenses all bingo related activities to ensure bingo games are conducted in accordance with the law. The agency licenses organizations, individuals, and entities to conduct bingo games, lease premises for the conduct of bingo, manufacture or distribute bingo supplies, and provide automated bingo system services. The table, *Bingo Licensees*, lists the types of licenses offered by the agency and the number of entities currently regulated.

<b>Bingo Licensees</b>	
<b>Types of Licenses</b>	<b>Number of Licenses</b>
Conductor	1,389
Commercial Lessor	449
Distributor	15
Manufacturer	15
System Service Provider	1

Groups eligible to conduct bingo include charitable organizations such as veterans organizations like the American Legion, religious societies like B’nai B’rith International, fraternal organizations like the Knights of

Columbus, volunteer fire departments, and groups supporting medical research or treatment programs. A breakdown of licensed charitable organizations by type is shown in the pie chart, *Licensed Conductors*. Bingo conductors must provide proof of charitable activities and must have a current 501(c) exemption from the Internal Revenue Service except religious societies and volunteer fire departments. Generally, a licensed organization may not conduct bingo games more than two times per day or three days per week, and individual games may not last more than four hours during a 24-hour period. The agency also issues temporary licenses to authorized organizations to conduct bingo as a one-time occasion.



### **Compliance and Enforcement**

The agency ensures licensees' compliance with the statute and rules, and the integrity and fairness of bingo games. The different types of audits and inspections conducted by agency staff are listed below.

- **Site Inspections** – Inspections of applicants to verify the location of the bingo premises and conduct pre-licensing interviews to explain bookkeeping responsibilities and determine the applicants' qualifications.
- **Books and Records Inspections** – Reviews of books and records designed to train a licensee in the proper method of establishing and maintaining bingo-related accounting records. Usually, new licensees receive this inspection six months after being licensed.
- **Tax Reviews** – Reviews of delinquent licensees that fail to file quarterly reports.
- **Assistance and Assessment Inspections** – Inspections to verify that organizations conduct bingo sessions in compliance with the statute and rules. Bingo auditors visit every licensed location once a year to conduct this inspection.
- **Audits** – Compliance and financial audits conducted when the agency finds serious discrepancies in a conductor's quarterly reports.
- **Compliance Reviews** – A hybrid of a compliance and financial audit that focuses on only one quarter to determine if organizations use charitable distributions for authorized charitable purposes.

★  
*The agency licenses  
 1,389 organizations  
 that conduct bingo.*

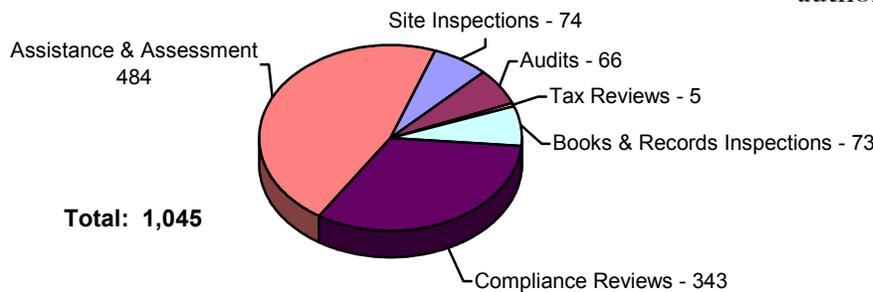
The pie chart on page 54, *Audit and Inspection Functions*, provides a breakdown of the agency's compliance monitoring activities in fiscal year 2003. Enforcement actions available to the agency when licensees fail to comply with bingo regulations include license denials, suspensions, and revocations. In addition, the Lottery Commission is authorized to assess administrative fines against licensees who commit violations such as failing to submit quarterly reports or remit prize fees to the agency. In fiscal year

2003, the agency settled five violations through agreed orders, revoked or suspended two bingo licenses, denied eight bingo licenses, and assessed fines against two licensees.

### Security

The Lottery Commission is responsible for protecting and maintaining the security and integrity of all lottery and bingo games, systems, and drawings. With the help of 31 commissioned peace officers, the agency handles administrative and criminal investigations relating to the lottery and bingo; and assists local, state, and federal authorities with investigations of possible criminal violations.

**Audit and Inspection Functions  
FY 2003**



The types of criminal violations relating to lottery and bingo include forgery, fraud, homicide, robbery, arson, and theft; and various forms of illegal gambling. The chart, *Security Activity*, provides

specific information about the agency's security activities in fiscal year 2003. If the security staff find administrative violations through these activities, it refers the cases to the agency's Legal Division for review and possible enforcement action by the Lottery Operations or Charitable Bingo Operations Divisions. The agency refers criminal cases to county and district attorneys for review.

The security staff conduct extensive criminal background checks on all lottery and bingo employees and licensees, oversee live lottery drawings, and maintain physical security at all agency locations. An in-house laboratory assesses security, quality, and environmental standards by testing a random sampling of lottery tickets and provides forensic analysis for questionable document verification. The security staff audit all lottery instant games to evaluate and approve the projected prize structure and parameters of each instant game to ensure its playability and integrity.

★  
*The security staff  
oversee all live lottery  
drawings.*

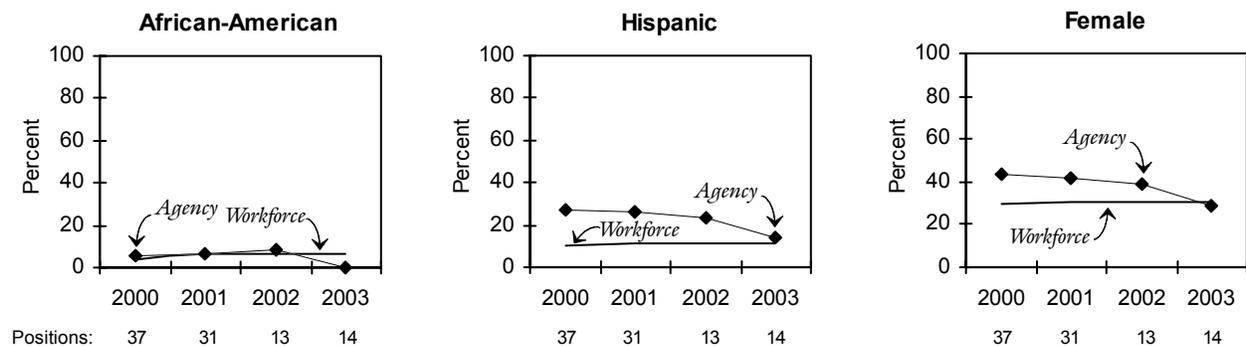
<b>Security Activity FY 2003</b>	
<b>Bingo</b>	
Complaints	212
Background Investigations	271
Required Inspections	2
Requests to Witness Destruction of Bingo Paper/Products	11
Bingo Occasion Inspections	44
<b>Total Investigations Initiated</b>	<b>540</b>
<b>Lottery</b>	
Complaints	588
Background Investigations	189
Retailer Inspections	727
Stolen Ticket Reports	1,168
<b>Total Investigations Initiated</b>	<b>2,672</b>

# APPENDICES

## Equal Employment Opportunity Statistics 2000 to 2003

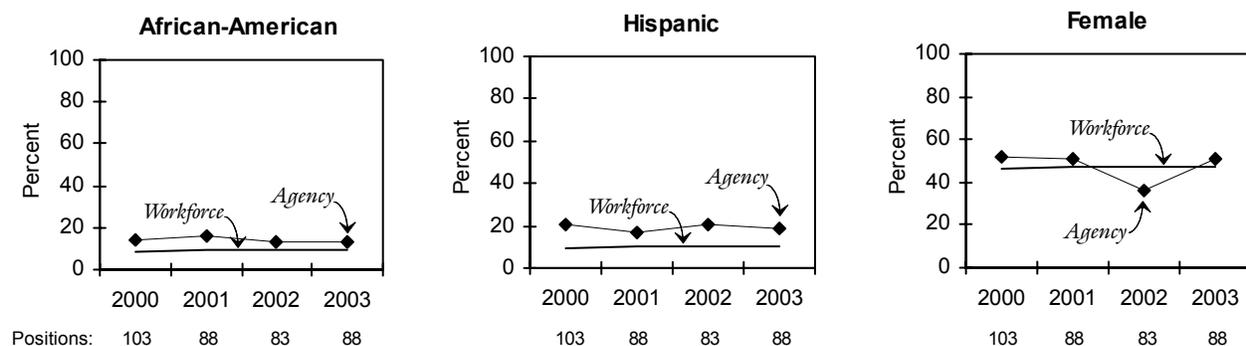
In accordance with the requirements of the Sunset Act, the following material shows trend information for the Texas Lottery Commission's employment of minorities and females in all applicable categories.<sup>1</sup> The agency maintains and reports this information under guidelines established by the Texas Commission on Human Rights.<sup>2</sup> In the charts, the solid lines represent the percentages of the statewide civilian workforce for African-Americans, Hispanics, and females in each job category. These percentages provide a yardstick for measuring agencies' performance in employing persons in each of these groups. The diamond-dashed lines represent the agency's actual employment percentages in each job category from 2000 to 2003. The agency does not employ persons in some job categories – skilled craft and service/maintenance.

### Administration



The agency's percentage of African-American, Hispanic, and female employees in this category has declined in recent years.

### Professional

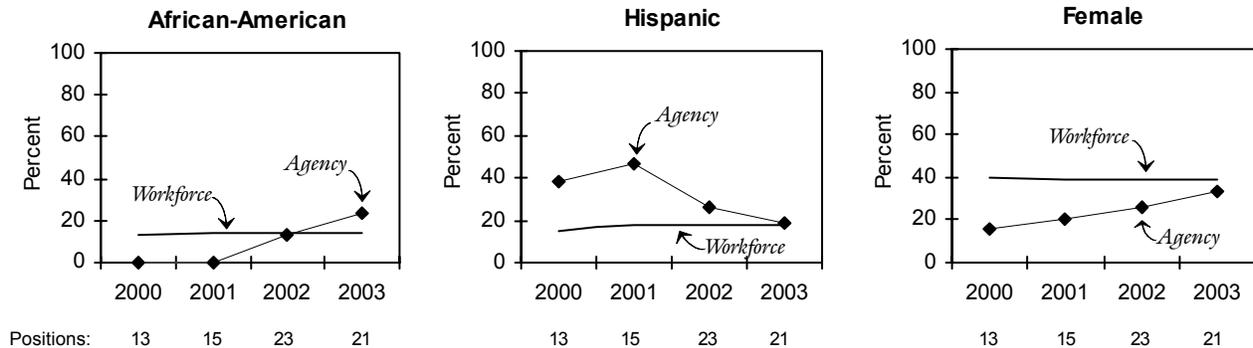


The agency generally exceeded the civilian labor force percentages for African-Americans, Hispanics, and females in this category.

# Appendix A

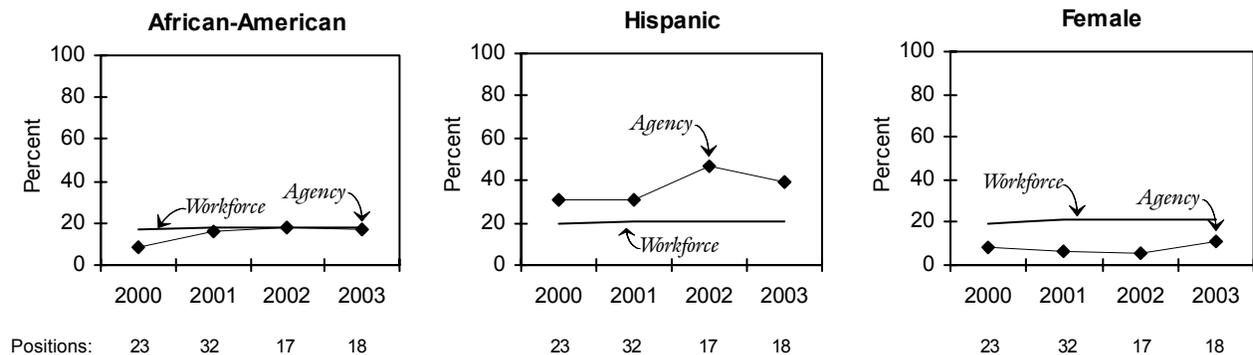
## Equal Employment Opportunity Statistics

### Technical Support



The agency improved its percentage of African-Americans in this job category, while its percentage of Hispanics has declined. The agency did not meet the civilian labor force percentage for females in technical support positions, but the agency's percentage has consistently increased.

### Protective Services

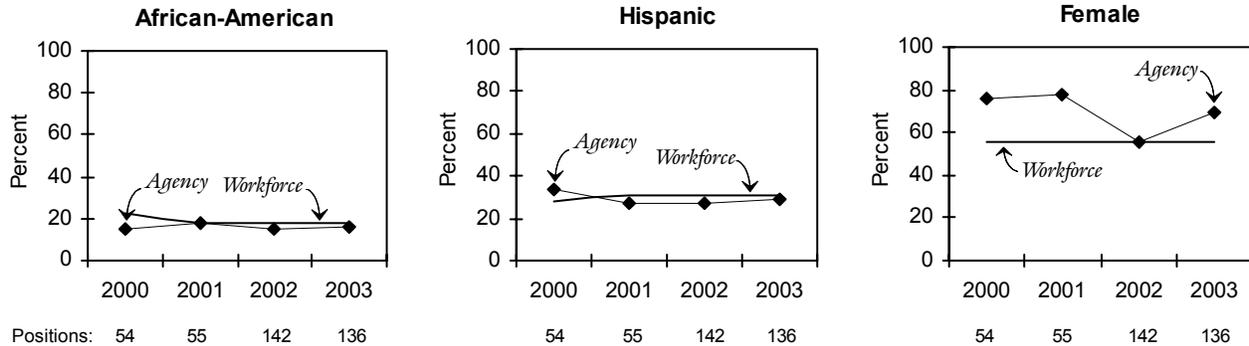


The agency improved its percentage of African-Americans in this job category, while consistently exceeding the civilian labor force percentage for Hispanics. The agency did not meet the percentage for females in protective services positions.

# Appendix A

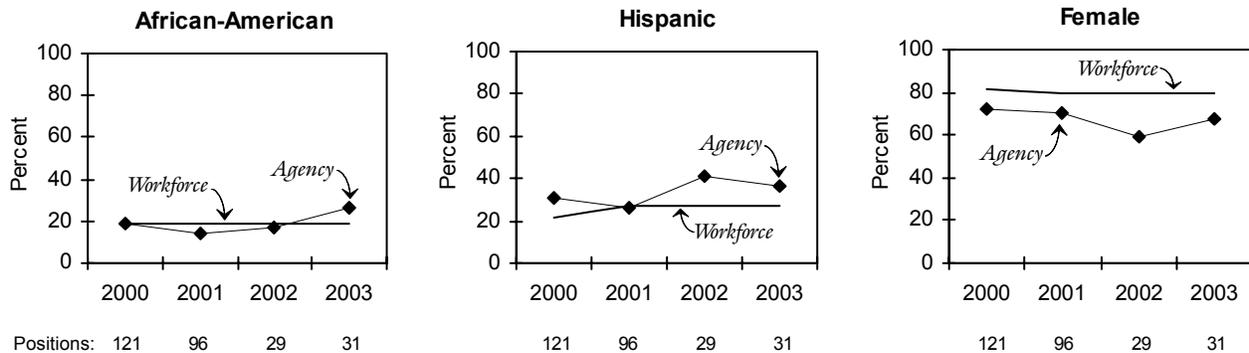
## Equal Employment Opportunity Statistics

### Para-Professionals



The agency fell slightly short of the civilian labor force percentages for African-Americans and Hispanics in this job category, but exceeded the percentage for females.

### Administrative Support



The agency fell short of the civilian labor force percentage for females, but improved its percentages of African-Americans and Hispanics.

<sup>1</sup> Texas Government Code, sec. 325.011(9)(A).

<sup>2</sup> Texas Labor Code, sec. 21.501. The Texas Human Rights Commission (HRC) has been the agency responsible for collecting and distributing EEO data. During the 2003 Session, the Legislature passed HB 2933 transferring the functions of HRC to a new civil rights division within the Texas Workforce Commission (TWC). The legislation is to take effect upon certification of the TWC civil rights division by the appropriate federal agency; no specific date has yet been established.

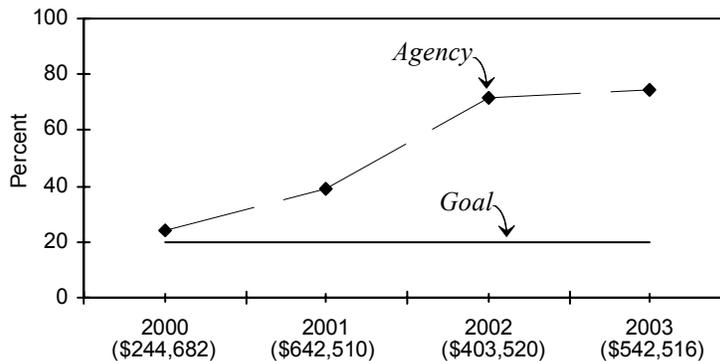


## Historically Underutilized Businesses Statistics 2000 to 2003

The Legislature has encouraged state agencies to increase their use of Historically Underutilized Businesses (HUBs) to promote full and equal opportunities for all businesses in state procurement. The Legislature also requires the Sunset Commission to consider agencies' compliance with laws and rules regarding HUB use in its reviews.<sup>1</sup> The review of the Texas Lottery Commission revealed that the agency is complying with state requirements concerning HUB purchasing.

The following material shows trend information for the Texas Lottery Commission's use of HUBs in purchasing goods and services. The agency maintains and reports this information under guidelines in the Texas Building and Procurement Commission's statute.<sup>2</sup> In the charts, the flat lines represent the goal for HUB purchasing in each category, as established by the Texas Building and Procurement Commission. The diamond-dashed lines represent the percentage of agency spending with HUBs in each purchasing category from 2000 to 2003. Finally, the number in parentheses under each year shows the total amount the agency spent in each purchasing category. The agency has fallen below the state goal for special trade and other services, but has generally surpassed the goal for professional services and commodities.

### Professional Services

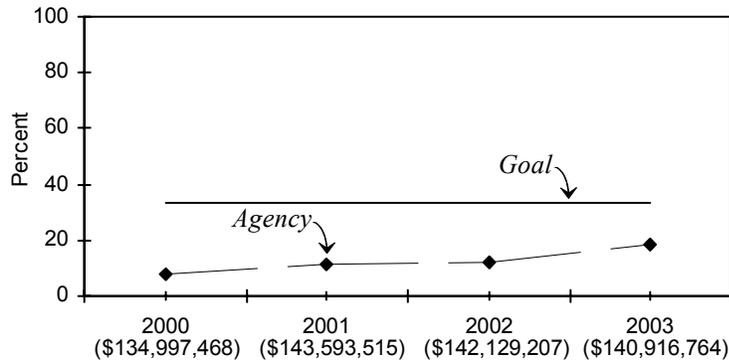


The agency has greatly exceeded the state goal for this category.

## Appendix B

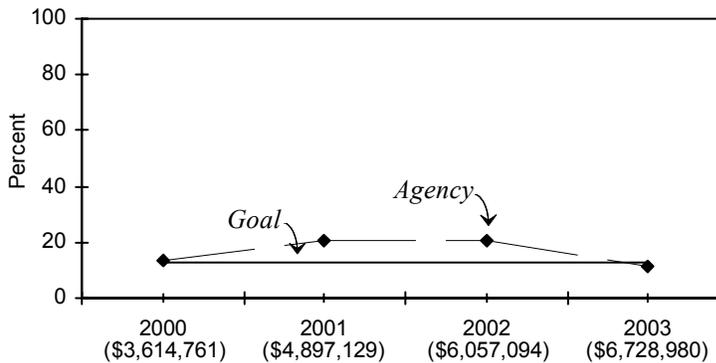
### Historically Underutilized Businesses Statistics

#### Other Services



The agency has consistently fallen below the state goal for this category. This category includes agency contracts for the lottery operator, instant ticket manufacturing, advertising, and other large contracts for the operation of the lottery.

#### Commodities

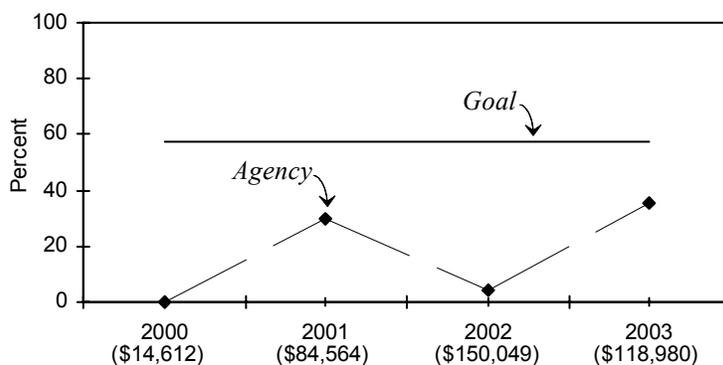


The agency has generally met or slightly exceeded the state goal for this category.

## Appendix B

### Historically Underutilized Businesses Statistics

#### Special Trade



The agency has consistently fallen below the state goal for this category.

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<sup>1</sup> Texas Government Code, sec. 325.011(9)(B).

<sup>2</sup> Texas Government Code, ch. 2161.



**SUNSET REVIEW OF THE  
TEXAS LOTTERY COMMISSION**

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