

SUBJECT: Continuing the Texas Lottery Commission

COMMITTEE: Licensing and Administrative Procedures — committee substitute recommended

VOTE: 7 ayes — Flores, Geren, Chisum, Goolsby, Hamilton, D. Jones, Quintanilla

0 nays

2 absent — Homer, Morrison

WITNESSES: For — Steve Bresnen, Bingo Interest Group; Joe Garcia, Trend Gaming Systems

Against — None

On — Dawn Nettles; Reagan Greer, Texas Lottery Commission

BACKGROUND: **Texas Lottery Commission.** In 1991, Texas voters approved a constitutional amendment authorizing a state lottery. In 1993, the 73rd Legislature created the Texas Lottery Commission to assume the administration of the lottery and to administer the Bingo Enabling Act.

Under Government Code, ch. 467, the commission comprises 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 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 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 lottery and the bingo divisions of the organization share the agency’s

security, legal, human resources, information technology, and other administrative functions.

In fiscal 2004, the agency had 325 full-time equivalent positions. The commission operated with a budget of \$193.7 million in fiscal 2003 — all of which came from lottery proceeds and bingo licensing fees. In fiscal 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 benefiting indigent health care. The remainder of the proceeds pays for prizes, the agency's administrative costs, and retailer commissions.

The Lottery Commission underwent Sunset review in 2002, and the Sunset Advisory 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 Lottery Commission is subject to the Sunset Act and will expire September 1, 2005, unless continued by the Legislature.

Charitable bingo. The Lottery Commission regulates charitable bingo under Occupations Code, ch. 2001. Since 1981, state licensed nonprofit organizations in Texas have been allowed to conduct bingo games following voter approval in local elections. Bingo proceeds must be spent for charitable purposes, although conductors of the games may deduct certain types of expenses before distributing money for charitable endeavors. In about 200 counties, bingo has been approved by one or more local jurisdictions. In 2004, charitable bingo generated about \$603 million in total gross receipts, of which about \$29.8 million was spent for charitable purposes.

The Lottery Commission, through its bingo division, regulates bingo and licenses the nonprofit organizations (called conductors), lessors of bingo halls, manufacturers and distributors of bingo supplies, and providers of automated bingo system services. Lessors can be either charities that lease space to other charities to hold bingo games or for-profit commercial lessors, which lease bingo halls to the nonprofit groups that operate the

games. The Lottery Commission regulates prizes, accounting methods, and other details of the games. In 2004, it commissioned about 1,419 charitable organizations to conduct bingo games.

Occupations Code, sec. 2001.101 establishes the types of organizations that can be licensed to conduct bingo. They include religious societies that have existed in Texas for at least eight years, certain nonprofit organizations that support medical research and treatment programs, nonprofit fraternal organizations, nonprofit veterans' organizations, and volunteer fire departments. Nonprofit organizations must have tax-exempt status under the U.S. Internal Revenue Code, sec. 501(c).

A 5 percent tax is imposed on prizes, of which counties and cities can choose to receive a portion. In 2004, \$21.3 million was collected in prize fees, of which about half went to local jurisdictions and about half to the state. In addition, a 3 percent gross rental tax is imposed on rental income received by people who lease premises for conducting bingo games.

DIGEST:

CSHB 1434 would continue the Texas Lottery Commission, the State Lottery Act, and the Bingo Enabling Act until September 1, 2017. The bill would apply or update standard Sunset provisions governing conflicts of interest, unbiased appointments to the agency's policymaking body, grounds for removing a board member, training of board members, complaint procedures, separation of policymaking and staff functions, public access through technology, public testimony at meetings of the board, and alternative rulemaking and dispute resolution procedures.

Expanding the size of the commission. CSHB 1434 would change the size of the commission from three to five members. The governor would appoint two additional members to the commission — one person to a term expiring on February 1, 2009, and the other to a term expiring on February 1, 2011.

Procurement. By repealing Government Code, sec. 2054.007(a), the bill would subject the lottery division to the general law governing purchasing and contracts by state agencies.

Major expenditures. Purchasing procedures established and evaluated by the executive director also would be established and evaluated by the commission. The bill would also include the commission in procurement decisions made by the executive director.

Business plan. The bill would direct the commission to develop a comprehensive business plan to guide major initiatives. Each year, the commission would assess the performance and value of each program and project described by the business plan. The business plan would have to include:

- a description of each program and project;
- relevant management information;
- financial data; and
- a detailed financial management plan.

Sales agent licenses. The bill would allow a sales agent's license to be transferred from one location to another under certain circumstances and would allow for a license that had been expired for not more than 10 days to renew under certain circumstances. The license amendment fee amount would need to be authorized by March 1, 2006. A sales agent, as well as an agency employee, also would be required to provide fingerprints and other identification to the commission upon request. The owner of a sales agent would be required to notify the director promptly when that person ceased to be an owner.

Complaints. CSHB 1434 would require the commission to analyze complaints in order to identify any trends or issues related to certain types of violations. The commission would set rules to require that the investigation of a complaint filed with the commission be completed within a reasonable time.

Consumer protection. The bill would require the commission to identify relevant laws governing consumer information and protection. The commission would be required to adopt policies ensuring compliance with those laws.

Definition of a minor. The bill would add a definition of "minor" to specify that a prize could be paid directly to a person age 18 or older.

Bingo licensing. The commission would establish comprehensive qualifications for licensure and renewal of licenses, develop a standard license renewal process, and establish standards of conduct for licensees. It would have to consider the compliance history of licensees when deciding whether to renew a license. The commission could deny a license renewal, after an opportunity for a hearing, if the licensee's compliance

history revealed conduct that was inconsistent with the statutes or the commission's rules. These rules would have to be adopted by March 1, 2006.

CASHB 1434 would require, instead of authorize, the commission to take certain actions when suspending or revoking a license for failure to comply with a code or rule violation or for a reason that would allow or require the commission to refuse to issue or renew a license in the same class and would establish a new option for a reprimand in these cases. The commission would be required to suspend, revoke, refuse to renew a licensee, or reprimand a licensee under these situations.

Changes in CASHB 1434 that govern the eligibility for licenses would apply only to the issuance or renewal of a license on or after the bill's effective date.

The bill would allow the commission to place on probation persons whose licenses were suspended. Persons with probated licenses could be required by the commission to report regularly to the commission, to limit their activities as required by the commission, or to take other reasonable actions to address their probation. The commission would have to adopt written guidelines to ensure probation was administered consistently and develop a system to track compliance with probation. These rules would have to be adopted by March 1, 2006.

The commission would be required to adopt rules to govern temporary suspensions. When considering the temporary suspension of a license, the commission would have to consider whether the continued operation of a license holder could constitute a financial loss to the state.

CASHB 1434 would establish procedures for the commission to follow when temporarily suspending a license of a bingo organization, including requiring that the commercial lessors and other bingo organizations involved with the suspended organization receive notice.

Upon a suspension of a bingo organization's license, the commission would be required to issue an amended or temporary license to other organizations that conduct bingo at the same location so they could conduct bingo during the time that the suspended organization conducted games. Limits on the number of temporary licenses an organization could have would not apply in this situation if certain conditions were met.

Schedule of sanctions — bingo. The commission would be required to adopt a schedule of sanctions that defined and summarized statutory and rule violations to ensure that sanctions were appropriate. The bill would establish requirements for how the schedule of sanctions would be structured. It also would establish a timeline both for licensees and the commission for the resolution of statutory and rule violations. This schedule and timeline would have to be adopted by March 1, 2006.

By March 1, 2006, the commission would adopt rules governing its monitoring of a license holder to determine compliance with statutes and rules.

Authorized bingo organizations. CSHB 1434 would eliminate current requirements that certain types of organizations be in existence for specified numbers of years to be authorized to conduct bingo. Instead, the commission could specify by rule the length of time that organizations must have been in existence. Rules concerning these requirements would have to be adopted by March 1, 2006.

Other provisions. CSHB 1434 would move the current requirement that the commission employ a bingo director to the law governing the commission and would give the director authority to enter into contracts, employ personnel, keep records, and administer the chapter.

The Bingo Advisory Committee, comprising members of the public and persons representing entities involved in bingo, would have to develop an annual work plan detailing the committee's objectives and issues to be addressed each year. CSHB 1434 specifies information that would have to be in the report.

CSHB 1434 would abolish regulations specifically for system service providers and the regulation of automated bingo services.

The bill would take effect September 1, 2005. Changes in the qualifications of commissioners, complaint investigation, and procurements would apply to appointments, complaints, and procurements made on or after the effective date.

SUPPORTERS
SAY:

Continuing the commission. The state lottery and bingo are important sources of revenue for the state, local jurisdictions, and charities. The lottery has contributed more than \$11 billion to the state since it was created. Without the revenue from these games, the state, charities and

local jurisdictions would be required to find other funding sources for a number of programs. The Lottery Commission is responsible for maximizing lottery revenue and ensuring that bingo revenue is spent on authorized purposes. The agency generally has been successful in accomplishing its mission and should be continued. There would be no significant operational or administrative efficiencies to be gained from restructuring.

Expanding the size of the commission. The work of the commission in operating the lottery and regulating charitable bingo is hampered by having only three commissioners. In the absence of one commissioner, for example, the other two could not informally discuss the work of the agency without violating the Open Meetings Act. Also because of its small size, the commission cannot form subcommittees to help it oversee the agency. The Lottery Commission is one of only eight boards or commissions appointed by the Governor that consist of three members, which limits the commission's effectiveness and internal communications.

Procurement. This agency, as with all state agencies, not only must be in step with rules, but also must project to the public that rules are being followed. By requiring the commission to adhere to the general law governing state agency purchasing and contracts, the bill would increase public trust that the commission was following legitimate business practices. The Lottery Commission should be aligned with standard operating procedures that govern all but a handful of state agencies.

Major expenditures and business plan. The commission should review and approve all major expenditures. It also should develop a comprehensive business plan, including a cost-benefit analysis, as a way to judge the ongoing effectiveness of its expenditures. The current lack of evaluation and planning could lead to excessive spending, duplicative efforts, or ineffective programs. The commission should review the business plan at least annually to assess the overall value of each project. Projects that failed to meet financial objectives should be adjusted or terminated. This would create a higher level of commission oversight over major expenditures and would reduce administrative costs.

Lottery retailer licenses. The changes in licensing provisions for lottery retailers would ensure greater accountability.

Complaints. The analysis of complaints could yield useful information. The data could help the commission educate licensees, focus on common problems, and change regulatory language to address new concerns. The commission should define by rule a reasonable length of time in which to conduct an investigation, which would be in step with a standard enforcement licensing model. These rules would protect the public and the licensee.

Definition of a minor. It is necessary to clarify the definition of a minor because current statute refers to a definition in the Property Code that describes a person younger than 21 years of age. This limit prevents people between the ages of 18 and 20 from receiving major winnings directly. Since people above the age of 18 legally are allowed to purchase lottery tickets, they should be able to receive any winnings as a result. The bill would resolve this conflict.

Bingo licensing. CSHB 1434 would make numerous changes to the commission's licensing procedures to ensure a consistent licensing process and to standardize enforcement provisions. These changes would help ensure that the procedures were fair to licensees, adequately protected the public, and safeguarded charitable revenue. The bill would achieve these objectives by requiring that the commission establish the qualifications for licensure and renewal so that all licensees were subject to the same requirements and aware of the qualifications.

The bill also would give the commission more flexibility to respond appropriately to licensees by authorizing a system of probation. The bill would require the commission to adopt rules governing temporary license suspensions to ensure that all suspensions were handled fairly and uniformly and to consider potential financial loss to the state when considering a temporary suspension. CSHB 1434 would require the commission to adopt a schedule of sanctions to apply to code and rule violations so that enforcements could be applied fairly and uniformly to licensees.

Requiring the commission to take action from a specified range when considering license revocations and suspensions would not harm the commission's ability to respond appropriately to individual situations and would not establish a bias toward sanctions. Provisions that required the commission to suspend, revoke, or refuse to renew a license would occur only after the commission had found a failure to comply with the code or a

rule or for other good cause. CSHB 1434 would ensure that action was taken in these situations but would leave the decision about the action to the commission.

Authorized bingo organizations. CSHB 1434 would eliminate the arbitrary requirements in current law that require different types of nonprofit organizations to have been in existence for various amounts of time before they could be licensed. For example, religious organizations must have existed in Texas for at least eight years, and fraternal organizations for three. There is no sound basis for these restrictions, and they serve no public protection purpose. CSHB 1434 would ensure that organizations wishing to conduct bingo were legitimate by authorizing the commission to establish standard time periods for organizations to have been in existence.

Other bingo provisions. CSHB 1434 would move the current requirement that the commission employ a bingo director and the director's current authority to administer the bingo division to a more logical place in statute and would give the bingo director the same general authority to do things given to other agency directors, such as enter into contracts, employ personnel, and keep records.

CSHB 1434 would help ensure that the Bingo Advisory Committee operated efficiently and effectively by requiring the committee to adopt an annual work plan.

OPPONENTS
SAY:

Continuing the commission. The Lottery Commission should be merged with the Racing Commission to form a new gaming commission. Alternatively, the operation of the lottery should be transferred back to the Comptroller's Office, allowing the agency to operate more independently. The regulation of bingo should be separated out.

Expanding the size of the commission. A three-member commission properly ensures that two commissioners cannot discuss business in a casual way outside of a formal meeting. This restriction assures the public that business is never discussed behind closed doors.

Procurement. The commission has managed well under the current procurement system. This system allows for time-sensitive purchases to be made quickly, for example. This can be important for the Lottery

Commission, which is more market- and business-oriented than other state agencies.

Bingo licenses. The commission should continue to be authorized, instead of required as in CSHB 1434, to take certain actions when it considers a license suspension or revocation. The bill would tie the hands of the commission by requiring that certain types of actions be taken, which in some cases may not be appropriate. These actions could trigger a series of events resulting in the use of less money for charitable purposes. For example, a revocation under the required conditions could lead to an action by the commission that resulted in a notation in a licensee's compliance history. To combat this, a licensee or organization might hire a lawyer and spend resources fighting a compliance history notation. It would be best not to change current law, which allows the commission more flexibility in handling license suspensions and revocations.

OTHER
OPPONENTS
SAY:

If more commissioners were added, the governor should appoint a representative who could speak for underprivileged people, who play the lottery in disproportionate numbers. This group should have a voice on the commission to address its concerns about the lottery.

If the Lottery Commission is to be expanded, it should include two representatives of bingo interests, instead of the one currently required. This would help ensure that the bingo industry is adequately represented.

The commission should have seven members. One or two public members should be lottery retailers and one or two other members should be individuals who were either lottery players with a full understanding of the games or "recovered gamblers."

Consumers should be required to present a valid ID prior to using gambling devices, such as scratch-ticket vending machines and self-service online ticket terminals, to ensure minors could not play these games.

Proposed rules changes should be posted on the agency's Web site on the day that they are proposed by the commission. This would make the Lottery Commission's rule-making process more accessible to the public. Also the comment period on proposed rules should be extended to from 30 days to 45 days or 60 days.

NOTES:

The committee substitute made a number of changes to the original, including:

- subjecting the commission to the general law governing purchasing and contracts by state agencies;
- allowing a sales agent's license to be transferred from one location to another under certain circumstances;
- requiring the director of the lottery division to determine the amount of the license amendment fee by March 1, 2006;
- amending the definition of a minor; and
- requiring the commission to issue amended or temporary bingo licenses to other organizations at the same location as an organization whose license was suspended.

The companion bill, SB 405 by Jackson, was reported favorably, as substituted, by the Senate Government Organization Committee on April 18.