

# INTRODUCTORY SECTION





## *Agency Vision, Mission and Values*

### **AGENCY VISION**

To be the preeminent Lottery and Charitable Bingo agency through innovative leadership.

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### **AGENCY MISSION**

Lottery Mission –

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.

Charitable Bingo Mission –

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.

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### **AGENCY CORE VALUES**

**Integrity and Responsibility** - The Commission works hard to maintain the public trust by protecting and ensuring the security of our lottery games, systems, drawings and operational facilities. We value and require ethical behavior by our employees, licensees and vendors. We promote the integrity of charitable bingo in Texas for the benefit of charitable organizations.

**Innovation** - We strive to incorporate innovation into our products to provide the citizens of Texas with the best entertainment experience available through our products. We pursue the use of technology that enhances the services that we provide to our customers and reduces our operating expenses.

**Fiscal Accountability** - We emphasize fiscal accountability by ensuring that all expenditures directly or indirectly generate revenue, enhance security, fulfill regulatory requirements, improve customer service and/or boost productivity. We recognize our responsibility in generating revenue for the

State of Texas without unduly influencing players to participate in our games. We maximize benefits to charities through the continual examination and review of charitable bingo operations.

Customer Responsiveness - The Commission takes pride in providing exemplary service to the people of Texas through the courteous dissemination of clear and accurate information about our products, services and regulatory functions. We seek and respond to feedback expressed by our employees, retailers, licensees and the playing and non-playing public. We apply this feedback in the development of our products and in the services that we provide.

Teamwork - We are committed to creating an environment of mutual respect where open, honest communication is our cornerstone. We embrace the diversity of our team and individual perspectives in working together to achieve our common goals.

Excellence - We strive for excellence by taking a position of leadership on issues that impact the Commission and achieve challenging goals by focusing on our core values.

December 20, 2005

To the Governor, Lieutenant Governor, Speaker of the House, Comptroller of Public Accounts, Members of the 79<sup>th</sup> Legislature, and Citizens of the State of Texas:

It is our pleasure to submit to you the Comprehensive Annual Financial Report (CAFR) for the Texas Lottery Commission (the "Commission") for the year ended August 31, 2005 with summarized comparative totals for the year ended August 31, 2004. In accordance with the Texas Government Code Chapter 466, the State Lottery Act, the report provides the Governor, legislators, oversight agencies, agency staff, citizens, and other interested parties with financial information and an overview of the Commission's operations. The Commission's management is responsible for the accuracy and completeness of the contents of this report.

This report was prepared in accordance with standards prescribed by the Governmental Accounting Standards Board (GASB), the Government Finance Officer Association of the United States and Canada (GFOA) and other rule-making bodies. We believe the report contains all disclosures necessary for the reader to understand the Commission's financial affairs.

The Commission's management has established a system of internal controls to reasonably safeguard the Commission assets from loss or unauthorized use or disposal; to provide reliable financial records for preparing internal and external financial reports and maintaining accountability over Commission assets; and to ensure compliance with applicable Federal and State laws, regulations and provisions of contracts and agreements.

The transmittal letter is designed to complement the Management Discussion & Analysis ("MD&A") and should be read in conjunction with it. The Commission's MD&A is located in the Financial Section immediately following the independent auditor's report.

## **PROFILE OF THE GOVERNMENT**

In November 1980, Texas voters approved a constitutional amendment authorizing charitable bingo on a local option basis. The first bingo licenses were issued in the spring of 1982. In November 1991, Texas voters approved a constitutional amendment authorizing a state lottery. The Texas Lottery began generating revenue for the State of Texas in 1992 as a division within the Comptroller of Public Accounts. The Texas Lottery Commission was formed as an independent agency on September 1, 1993. Regulatory authority for Charitable Bingo was transferred to the Texas Lottery Commission effective April 1, 1994.

The Commission has two main functions:

- 1) The Commission, under the authority granted the agency by the State Lottery Act, administers the Texas Lottery games in an efficient and secure manner using appropriate marketing tools and innovative technology to generate revenue for the State of Texas while enhancing public confidence in the integrity and fairness of the games.
- 2) The Charitable Bingo Operations Division is charged under the Bingo Enabling Act with the regulation and administration of all charitable bingo-related activities in the State of Texas, and contributes to the regulatory and tax and revenue collection functions of the agency. The Division licenses all bingo-related activities, collects taxes and prize fees generated from the conduct of charitable bingo, audits bingo licensees, conducts tests on bingo products intended for use in Texas, such as bingo paper, pull-tabs and electronic equipment, and makes quarterly allocations to local units of government for their share of the prize fees collected.

The three-member Commission sets policy, promulgates rules for the agency, and performs all other duties required by law. The Governor appoints Commission members, with the advice and consent of the Senate, to staggered six-year terms. One member must have experience in the bingo industry.

The agency is divided into 8 divisions: Executive, Charitable Bingo Operations, Internal Audit, Lottery Operations, Administration, Legal Services, Media Relations and Governmental Affairs. Except for the Executive Director, Charitable Bingo Operations Director, and Internal Audit Director, who report directly to the Commissioners, each division director reports to the Deputy Executive Director, who reports to the Executive Director.

## **Products and Services**

### ***Texas Lottery***

The *Games of Texas* are the body of Texas Lottery<sup>®</sup> games that the Commission makes available to the playing public through more than 16,000 licensed Lottery retailers.

These include instant, or “scratch-off,” games and on-line games.



Instant games are played by scratching off a latex covering on each ticket to see if a prize has been won. A variety of themes, play styles and prize structures are available in a constantly revolving lineup of approximately 80 games. Players enjoy multiple chances and multiple ways to win on each ticket, as well as the immediate gratification of winning a prize.

On-line games are those games in which tickets are generated from a terminal connected to a central system and a drawing is held to determine a set of winning numbers. The Texas Lottery currently offers five on-line games: *Mega Millions* with the add-on Megaplier feature, *Lotto Texas*, *Pick Three*, *Cash Five*, and *Texas Two Step*. Texas joined *Mega Millions* in October 2003, marking the first time that Texas has ever participated in a multistate lottery game.



**Mega Millions™** - A twice-weekly multistate on-line game that features a 5-of-52 plus 1-of-52 bonus-ball-style matrix in which players select 5 numbers between 1 and 52 plus the bonus ball number for a chance to win a multi-million-dollar jackpot prize. The jackpot prize starts at \$12 million. When no ticket matches all six numbers drawn, the jackpot increases for the following draw. The Megaplier™ feature of the *Mega Millions* game allows players the opportunity to wager an extra \$1 per playboard for a chance to increase their non-grand/jackpot prize winnings by 2, 3 or 4 times depending upon the Megaplier number drawn.



**Lotto Texas™** – A twice-weekly on-line game that features a 5-of-44 plus 1-of-44 bonus-ball-style matrix in which players select five numbers between 1 and 44 plus the bonus ball number for a chance to win a multi-million dollar jackpot prize. When no ticket matches all six numbers drawn, the jackpot increases for the following draw.



**Texas Two Step®** – A twice-weekly on-line 4-of-35 plus 1-of-35 bonus ball game. Players select four numbers plus a bonus ball number for a chance to win a jackpot prize. Jackpots start at \$200,000 and there are seven different ways to win.



**Pick 3™** – A twice-daily on-line game (12 drawings a week) with a top prize of \$500 on a \$1 wager.



**Cash Five™** – A daily on-line game with a 5-of-37 lotto-style matrix. All prizes are pari-mutuel (except for matching 2 of 5, which pays a guaranteed \$2). If no ticket matches all five numbers drawn, the prize pool for the top 5-of-5 prize is allocated or rolls down to the 4-of-5 prize (i.e., does not carry forward).

### **Charitable Bingo**



The Charitable Bingo Operations Division licenses bingo conductors, lessors, manufacturers, distributors, and system service providers. Charitable bingo conductors in Texas consist of nonprofit organizations such as veterans' organizations, religious societies, fraternal organizations, volunteer fire departments and groups supporting medical research programs.

Charitable bingo has positive benefits for charities, players, and state, county and municipal governments in Texas through gross receipts from the conduct of charitable bingo, bingo prizes awarded, and charitable distributions. Distributions by organizations conducting charitable bingo benefit the people of Texas in many ways that include providing assistance to local libraries, veterans organizations, museums, women's shelters, needy children, the disabled, homeless shelters, churches, schools, drug and alcohol treatment programs, medical treatment and research programs,

volunteer fire departments, EMS units, police officer organizations, and senior citizen organizations, to name a few.

## **Populations Served**

The Commission serves a number of direct and indirect customers. The primary direct customers of the Texas Lottery Commission include lottery players and licensed retailers, charitable bingo players and licensees, advisory groups and vendors. Indirect customers are those Texas populations that benefit from the conduct of the *Games of Texas* and Charitable Bingo, from the agency's net revenue contributions to the State of Texas, and from associated agency activities that serve the public good.

The lottery player base consists primarily of adult Texans 18 years and older, as well as similar-aged players from surrounding states and Mexico who travel to Texas to purchase lottery tickets. The charitable bingo player base consists primarily of adult Texans 18 years and older; however, it is not required that a bingo player be 18 if accompanied by an adult. Detailed demographic information is provided in the Statistical Section.

## **Budget Process**

The Texas Legislature establishes the agency's appropriations, and certain key performance measures, on a biennial basis. The agency's budget is prepared with direct input from division management and is reviewed and approved by the Executive Director or Charitable Bingo Operations Director, as applicable, through a series of internal budget hearings held with each division director regarding the respective budget requests. The three-member Commission reviews the final budget requests before submission to the legislative oversight agencies and the Governor. The agency uses performance measures and goals to determine where resources are needed and adjusts priorities accordingly.

## **ECONOMIC CONDITION AND OUTLOOK**

State lotteries have progressed from nonexistent to pervasive in just 41 years since New Hampshire became the first state to enact a state-run lottery in 1964. Texas became the 35<sup>th</sup> state to legalize lottery operations in 1992. Today, nearly 40 states conduct lotteries. Charitable bingo and/or other charitable gaming activities are legal in 46 states and the District of Columbia.

Economic trends and fluctuations can have a considerable impact on the agency's ability to generate revenue for the State of Texas through the conduct of the *Games of Texas* and charitable bingo. Alternative gaming venues can have an impact as well, by capturing the entertainment dollars of potential lottery and charitable bingo players. Charitable bingo and Lottery products compete in a mature yet dynamic market for the discretionary entertainment dollars of primarily Texans over 18 years of age. The Commission strives to provide the citizens of Texas with the best entertainment experience available through its products. Periodically, changes are recommended to keep the games innovative and exciting for Texas players.

New and potential technologies, game innovations and legislative changes present a dynamic environment for the Commission and its industry in future years. The Commission responded to legislative authorization to engage in multi-jurisdictional gaming by agreeing to join the *Mega Millions* game, which was launched in Texas in late 2003. In addition, in an effort to attract a larger portion of the market, the Commission is exploring the possibility of joining another multi-

jurisdictional game. The Charitable Bingo Operations Division continues to explore avenues to increase bingo attendance and yield incremental value to the charities for which they operate. Additional trends occurring in the gaming industry include Internet gaming, video lottery terminals, Keno and linked bingo games.

## **AWARDS AND ACKNOWLEDGEMENTS**

### **GFOA Certificate of Achievement**

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to the Texas Lottery Commission for its comprehensive annual financial report for the fiscal year ended August 31, 2004. This was the third consecutive year that the Commission has received this prestigious award. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both generally accepted accounting principles and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe that our current comprehensive annual financial report continues to meet the Certificate of Achievement Program's requirements and are submitting it to the GFOA to determine its eligibility for another certificate.

### **Independent Audit**

Texas statutes require an annual financial audit by an independent Certified Public Accountant. The independent auditors' opinion on the Commissions financial statements is included in the financial section of this report.

### **Acknowledgements**

The preparation of this report would not have been possible without the efficient and dedicated services of the Lottery Commission staff within the Office of the Controller Division. We would also like to express our appreciation to other staff within the Texas Lottery Commission who assisted and contributed to the preparation of this report.

Sincerely,

Gary Grief  
Acting Executive Director



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## COMMISSION OFFICIALS

A three member commission, who are appointed by the Governor to 6-year staggered terms, head the Commission. The officials, their terms of office and hometowns are:

C. Tom Clowe, Jr.	November 13, 1998 - February 1, 2005	Waco, Texas
James A. Cox, Jr.	June 3, 2002 - February 1, 2009	Austin, Texas
Rolando Olvera, Jr.	August 28, 2003 - February 1, 2007	Brownsville, Texas

### **Chairman Clowe**

Mr. Clowe is retired after a highly successful career as a business executive. He served as Senior Vice President of Southern Union Company in Austin. He joined Missouri Gas Energy, a division of Southern Union Company, as its President and Chief Operating Officer.

Mr. Clowe was Chairman of the Board, President and Chief Executive Officer of Central Freight Lines, Inc. Mr. Clowe has served as Chairman of the Texas Motor Transportation Association, Chairman of the Tank Truck Conference of the American Trucking Association, and Regional Vice President of the American Trucking Association. He was employed by the Texas Railroad Commission and was appointed as its first Executive Director in the Commission's 97-year history.

Mr. Clowe received a bachelor's degree in business administration from the University of Texas at Austin and has completed several graduate-level management courses at Harvard Business School.

Mr. Clowe was appointed to the Commission on November 13, 1998 by Governor George W. Bush. Governor Bush appointed him as chair of the Commission on March 21, 2000. Mr. Clowe's term on the Commission expired February 1, 2005. Mr. Clowe continues to serve at the pleasure of the Governor.

### **Commissioner Cox**

Mr. Cox is a certified public accountant and former President and Chief Executive Officer of Hydrolab Corporation. He previously served as President of the Resort and Aviation Groups of the Estate of Howard Hughes, and as an accounting and auditing partner of Deloitte & Touche. He was a member of the Texas General Services Commission from 1999 to 2002.

Mr. Cox received a bachelor's degree and master's degree from the University of Texas at Austin, where he is currently pursuing a doctorate in American Civilization. Mr. Cox is a member of the American Institute of Certified Public Accountants and the Texas Society of Certified Public Accountants.

Governor Rick Perry first appointed Mr. Cox to the Commission on June 3, 2002. Mr. Cox was reappointed by Governor Perry on March 4, 2003 for a term to expire February 1, 2009.

### **Commissioner Olvera**

Judge Olvera is a former Texas State District Judge and is currently an Attorney/Mediator/Arbitrator and managing partner with the Brownsville law firm of Spain & Olvera. He is a member of the State Bar of Texas, the Cameron County Bar Association, the Hidalgo County Bar Association, and a fellow with the Texas Bar Foundation.

Judge Olvera received a bachelor's degree from Harvard University, and a doctorate of jurisprudence law degree from the University of Texas School of Law.

Judge Olvera was appointed to the Commission on August 28, 2003 by Governor Rick Perry. Judge Olvera's term on the Commission expires February 1, 2007.

## **AGENCY OFFICIALS**

### **Acting Executive Director**

Gary Grief is the Acting Executive Director of the Commission, and functions as the Chief Executive Officer. Mr. Grief was named to this position on July 11, 2005 by the three-member Texas Lottery Commission, which is appointed by the Governor. Mr. Grief has been with the Commission since 1992 and previously served as Acting Executive Director from September 2002 to February 2003.

Mr. Grief joined the Commission as the statewide Claim Center Supervisor in May 1992, and was later named Lottery Operations Director in 1997. He was named Deputy Executive Director of the agency in February of 2003 and oversaw the day-to-day operations of the Commission.

### **Director of Charitable Bingo Operations Division**

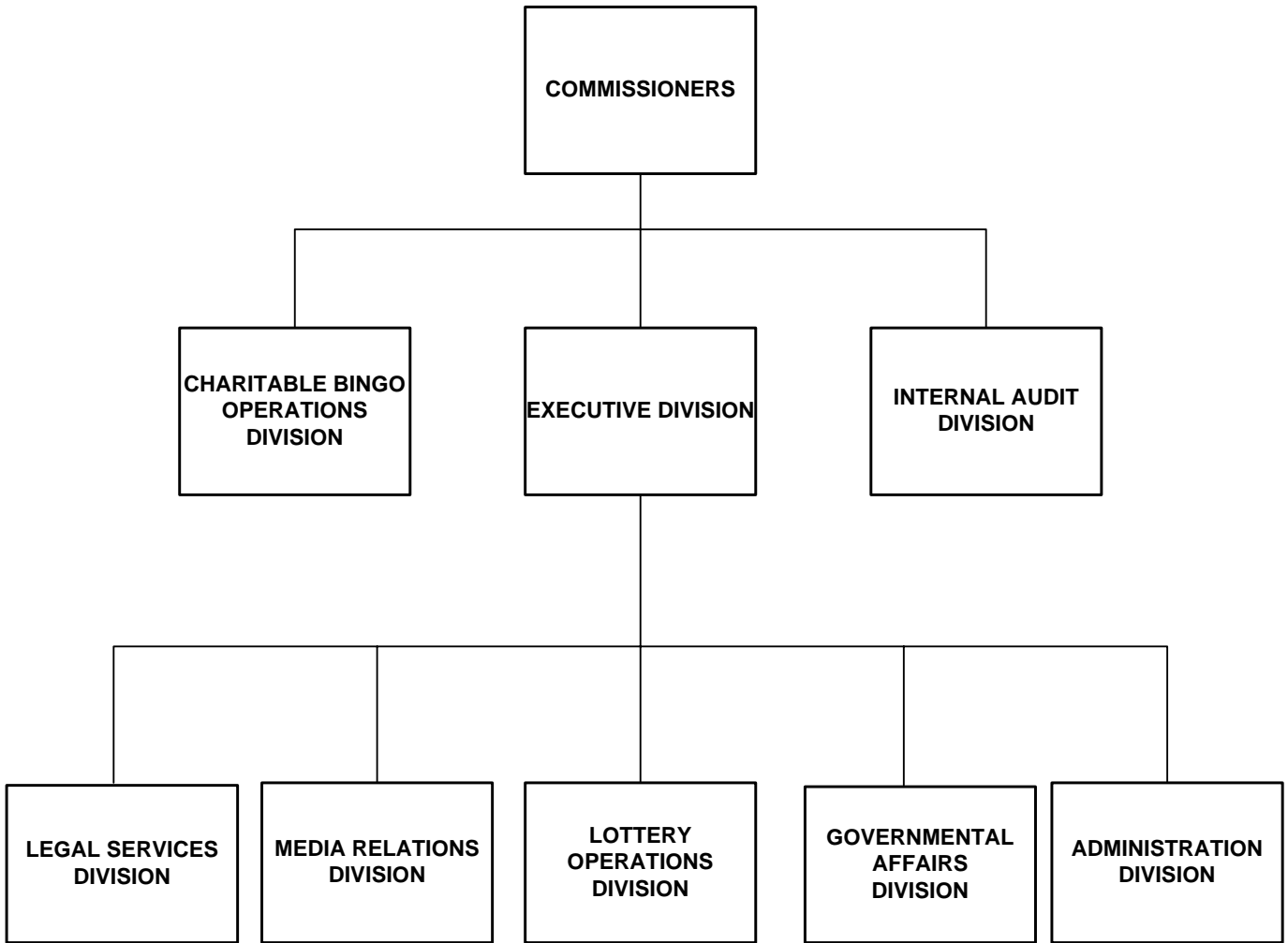
William Lee (Billy) Atkins was appointed Charitable Bingo Operations Director by Texas Lottery Commissioners on Thursday, October 29, 1998. Prior to that, Mr. Atkins served as both Acting Director and Assistant Director of the Charitable Bingo Division of the Commission.

Mr. Atkins first came to the Commission as the Special Projects Coordinator for the Intergovernmental Affairs Section in January 1993, a position he held until April 1994.

Prior to working at the Commission, Mr. Atkins was a Legislative Assistant for Texas Senate Senator John T. Montford from January 1983 to December 1985. In January 1987 he worked as an Administrative Assistant for Texas State Representative Gary L. Watkins until December 1992.

Mr. Atkins is currently President of the North American Gaming Regulators Association (NAGRA), a professional organization of federal, state, provincial, local, and tribal government agencies primarily responsible for regulation of legalized gaming activities.

**TEXAS LOTTERY COMMISSION'S ORGANIZATIONAL STRUCTURE**



# Certificate of Achievement for Excellence in Financial Reporting

Presented to

## Texas Lottery Commission

For its Comprehensive Annual  
Financial Report  
for the Fiscal Year Ended  
August 31, 2004

A Certificate of Achievement for Excellence in Financial Reporting is presented by the Government Finance Officers Association of the United States and Canada to government units and public employee retirement systems whose comprehensive annual financial reports (CAFRs) achieve the highest standards in government accounting and financial reporting.



*Nancy L. Zjelke*

President

*Jeffrey R. Enos*

Executive Director