

**REPORT OF THE
GOVERNOR'S COMMISSION ON THE LOTTERY**

FEBRUARY 2, 1989

February 2, 1989

The Honorable Rudy Perpich
130 State Capitol
St. Paul, Minnesota 55155

Dear Governor Perpich:

On December 8, 1988 you appointed a commission to make recommendations to you and to the legislature on the structure and operations of a state lottery. Today I am pleased to present you with the findings and recommendations of the commission.

The recommendations of the commission stem from four basic conclusions. First, we believe that Minnesotans approved the lottery both for its value as entertainment and as a means of raising money for the state. Second, we believe that to accomplish these aims the lottery must be run as a business and must be given the flexibility to make sound business decisions. Third, we believe that lottery legislation must provide sufficient safeguards to protect both the financial and moral reputation of the state. Fourth, the lottery must be structured in such a way that no business or organization is at an a priori advantage or disadvantage when they wish to do business with the lottery.

Over the past six weeks the commission has put in long hours on this issue and has learned much. I would like to thank my fellow members for the time and effort they have devoted to this report and I would like to thank you for giving us the chance to serve.

We stand ready to discuss our findings with you and with members of the legislature as you see fit.

Sincerely,



Gene A. Bier
Chair

MEMBERSHIP

Gene A. Bier, Plymouth
Chair

Erwin L. Goldfine, Duluth

Wes D. Lane, Eagan

John C. Lynch, Willmar

John D. Milne, Mendota Heights

Bob R. Regalbuto, St. Paul

James C. Selmer, St. Paul

Elwyn G. Tinklenberg, Blaine

Judith K. Wickhorst, Hastings

GENERAL FINDINGS

- Minnesotans voted for a lottery both for its entertainment value and as a means of raising money for the state. The commission believes that it was clear to the public that raising money for state programs was a major goal of the sponsors of the ballot initiative.
- The goals of providing entertainment and raising money for the state are not incompatible. A lottery which attracts the greatest consumer interest will likely also be that which is the most successful at raising money.
- The lottery is unlike any current state enterprise. In most, though not all, respects, it more closely resembles a business and should be run as such.
- As the Constitution specifies that only a state-run lottery is permitted, sufficient oversight must be provided so that lottery operations are consistent with the dignity and fiscal responsibility of state government.
- It is essential to the security and reputation of the lottery that no potential contractor, supplier, or ticket sales agent be at an inherent advantage or disadvantage in competing for lottery business. All who wish to do business with or for the lottery should be able to do so fairly and evenly.

ORGANIZATION

FINDINGS

- The mission of the lottery is unlike that of any other state agency. While it is expected to deliver a service it is also expected to turn a profit. As such, its mission differs from that of existing agencies.
- A lottery differs from the agencies supervising charitable gambling and parimutuel racing in that it has operational and service delivery responsibilities while the primary responsibilities of the Charitable Gambling Control Board and the Minnesota Racing Commission are regulatory. In addition, the commission does not believe that creating another layer of government at this time would enhance the operations of any of the three gambling-related agencies.
- Initiating a lottery will place great demands on those responsible for its management. These demands could seriously detract from the mission of any existing agency charged with managing or overseeing the lottery.

RECOMMENDATIONS

- The commission recommends:
 - *That the lottery be independent of other state agencies, including other gambling-related agencies;*
 - *That in order to assure proper oversight and security the lottery be operated as a state agency rather than as an independent chartered corporation or under contract to a private business. The commission believes that either of these two options would give too much power to too few people;*
 - *That the day-to-day operations of the lottery be controlled by a director appointed by the governor with the advice and consent of the Senate and serving at the pleasure of the governor;*

- *That the general policy of the lottery be reviewed by a board representative of the citizens of Minnesota;*
- *That this board be composed of between five and seven members appointed by the governor with the advice and consent of the Senate;*
- *That in order to ensure the board remains representative of the citizens of the state while maintaining continuity of operations members serve no more than two four year terms and that no more than two terms of office expire in any one year;*
- *That membership on the board be divided as evenly as possible between residents of the Twin Cities metropolitan area and Greater Minnesota;*
- *That the board have the power to review and approve an organizational and annual business plan prepared by the director, the lottery budget, financial reports submitted by the director, and any rules promulgated by the director, including game rules;*
- *That game rules not be subject to the administrative procedures act.*
- *That the legislature set compensation for the board at a level commensurate with the Charitable Gambling Control Board, the Minnesota Racing Commission, and other state boards and commissions. However, the commission is concerned that current levels of compensation for members of boards and commissions preclude the service of some Minnesotans on these organizations, and recommends that the legislature review the current compensation policy.*

FINDING

- In order to serve both the desire of the people for entertainment and the need of the state for revenue, the director should be given maximum flexibility for operations consistent with the need to preserve the reputation, dignity, and financial security of the state.

RECOMMENDATIONS

- The commission recommends:
 - *That the internal organization of the lottery be left to the discretion of the director rather than specified in legislation;*
 - *That all employees of the lottery except for management, sales, distribution, and security personnel be in the classified civil service;*
 - *That as many major items purchased by the lottery are unlikely to be familiar to state purchasing agents the lottery be required to follow state procurement procedures, but be allowed to do its own procurement consistent with these procedures;*
 - *That major purchases and contracts by the lottery require review by the lottery board;*
 - *That the legislature should not dictate the number and size of prizes, but that the appropriate distribution of the number and size of prizes be determined by the marketplace;*
 - *That the lottery be required to return a minimum of fifty percent of total annual sales revenues to the players as prizes. The commission believes that a higher return to players may prove optimal both to the players and to state revenues, but also believes that initially the lottery management should be given the discretion and flexibility to seek the optimal level of return.*

ADVERTISING

FINDINGS

- As with any consumer good or service, informational advertising is necessary to the success of the lottery.
- The dignity and reputation of the state requires that advertising be conducted in good taste, and not mislead the public.
- Specific restrictions on advertising are likely to interfere with the lottery's ability to do business without protecting the public interest.

RECOMMENDATIONS

- The commission recommends:
 - *That legislation require that advertising of the lottery be consistent with the dignity of the state and also require that the odds of winning each prize be prominently posted at every place of lottery ticket sale;*
 - *That the lottery board be required to adopt an advertising code of ethics. This code must require that lottery advertising is accurate and not misleading, and that lottery advertising not exploit specific groups or economic classes of people;*
 - *That all advertising campaigns be reviewed and approved by the lottery board for conformance to the code before being released to the public.*

TYPES OF GAMES

FINDINGS

- The goals of the lottery require that a variety of lottery games be available to the public, as long as the security of the games is ensured and the selection of winners is truly random.

RECOMMENDATIONS

- The commission recommends:
 - *That the legislature not restrict the types of lottery games with the following exceptions:*
 - *All games must require a random selection of winners;*
 - *The lottery should not operate pulltabs, tipboards, bingo, and other games now used by charitable gambling organizations;*
 - *Persons under the age of 18 should not be permitted to purchase lottery tickets;*
 - *No terminal or device should be used for any lottery game which may be operated solely by the player without the assistance of the retailer, and that no terminal or device used for a lottery game dispense coins or currency.*

SECURITY

FINDINGS

- The security of the lottery is the single most important element in maintaining both the success of the lottery and the reputation and financial security of the state.

RECOMMENDATIONS

- The commission recommends:
 - *That the background of potential employees, sales agents and major contractors and suppliers be checked for criminal activity, record in meeting previous contractual arrangements, and tax or other money owed to the state;*
 - *That lottery security staff be given the authority to access the records necessary to conduct background investigations;*
 - *That the lottery be required to conduct an annual outside independent audit. This audit should be completed within 90 days after the end of the fiscal year;*
 - *That the director be required to make a quarterly report of lottery expenditures and revenues to the board, the governor, and the legislature;*
 - *That the director be required to retain complete financial records for a period of five years;*
 - *That the employees of the lottery and of its major contractors and suppliers and the members of their immediate families not be permitted to win lottery prizes;*
 - *That all sales of lottery tickets be on a cash-only basis.*

TICKET AGENTS

FINDINGS

- The commission believes that a strong network of lottery sales agents from the private and nonprofit sectors is critical to the success of the lottery. Such a network should include a wide range of types of outlets and should be accessible to citizens in all parts of the state.
- The commission recognizes the role played by charitable gambling in Minnesota communities and also recognizes the potential for conflict between a lottery and charitable gambling. The commission was unable to find evidence that lotteries had hurt charitable gambling revenues in any state where they coexist. However, the commission also recognizes that there are substantial differences between charitable gambling in Minnesota and that in other states.
- With the exception of potential conflicts with charitable gambling, the commission could find no reason to exclude any category of business or nonprofit organization from selling lottery tickets. However, the commission also believes that the integrity and security of the lottery are best served when the lottery does not account for a major portion of an organization's business.

RECOMMENDATIONS

- The commission recommends:
 - *That any Minnesota retail business or nonprofit organization possessing a sales tax permit be eligible to become a lottery sales agent;*
 - *That the director have the authority to select sales agents based on sound business practices while assuring reasonable geographic access to a sales agent by all Minnesotans;*
 - *That no sales agent be solely or primarily in the business of selling lottery tickets.*

- That to protect charitable gambling interests no on-sale liquor establishment which has housed a charitable gambling facility within the previous five years be eligible to become a lottery sales agent.*

COMPULSIVE GAMBLING

FINDING

- The commission finds little evidence that state lotteries make a strong contribution to compulsive gambling, particularly when compared with other types of gambling now available in Minnesota. However, the commission also believes that as the lottery may make a minor contribution to the problem, it should help contribute to the solution.

RECOMMENDATION

- *The commission recommends that some portion of lottery proceeds be used to help fund a treatment program for compulsive gambling.*

TAXATION

FINDING

- The commission can find no compelling reason to treat the taxation of prizes won in a state lottery differently than those won through parimutuel racing or other forms of gambling.

RECOMMENDATIONS

- The commission recommends:
 - *That lottery winnings be taxed at a level determined by the legislature;*
 - *That the state have the power to withhold lottery winnings to satisfy back taxes or other debts owed the state, arrearage in child support or alimony, or other legal judgements against a winner's assets;*
 - *That lottery tickets not be subject to the state's sales and use tax.*

BUDGET

FINDING

- While legislative oversight over the lottery budget is desirable to enhance the security and reputation of the state and the lottery, the need for flexibility in the lottery business and the unpredictability of some expenses require that some items be exempt from the biennial appropriations process.

RECOMMENDATION

- *The commission recommends that the lottery director be empowered to expend funds to pay prize winners, commissions to sales agents, and to purchase and promote lottery games and game-related services, and that these funds be made available from lottery sales without appropriation by the legislature.*

REVIEW OF LOTTERY OPERATIONS

FINDING

- The commission recognizes that operating a lottery is new to Minnesota. While operations in other states provide a model, there is no guarantee that this model will be perfectly adaptable to Minnesota. The commission therefore believes that, after sufficient time has passed to permit the lottery to acquire a track record, the legislature and governor be required to review lottery operations and organizations.

RECOMMENDATION

- *The commission recommends that legislation authorizing a lottery provide for a thorough review of lottery organization and operations five years after the sale of lottery tickets begins.*

STARTUP

FINDING AND RECOMMENDATION

- Voter approval of a lottery suggests that many Minnesotans are anxious to participate in a state lottery. The commission therefore urges the legislature to pass enabling legislation this year and that the lottery board and director be asked to begin operations as soon as possible consistent with sound and secure business practices.