

Regulatory Structure Review of Charitable Gaming in Virginia

HB1800 Line Item 105 D1

Adam J. Tagert, CIA CIGA CGAP

Audit Manager

October 14, 2021

OFFICE OF THE STATE INSPECTOR GENERAL

OVERVIEW

- **HB 1800 (Chapter 552 of the Acts of Assembly)**
- **OSIG Findings & Recommendations**
- **VDACS' Observations**
- **Conclusions**
- **Takeaways**

HB 1800 LINE ITEM 105 D1

The Office of the State Inspector General shall, with the assistance of the Office of Charitable and Regulatory Programs, review the regulatory structure of charitable gaming in Virginia, to include, at a minimum:

HB 1800 LINE ITEM 105 D1 (CONT.)

- i. Current permitting requirements and exemptions;**
- ii. Net revenue dedicated to charitable activities and which types of gaming revenue is excluded from this calculation;**
- iii. Charitable gaming occurring in remote locations not located in the same jurisdiction as the registered address of the charitable organization;**
- iv. Enforcement of the “social quarters” and “members and guests” limitation;**

HB 1800 LINE ITEM 105 D1 (CONT.)

- v. The structure of the Charitable Gaming Board including any changes needed to prevent conflicts of interest;**
 - vi. The adequacy of enforcement and resources dedicated to oversight activities of the Office of Charitable and Regulatory Programs; and**
 - vii. Whether regulation of charitable gaming would be more appropriately vested with the Virginia Lottery**
- The Office of the Inspector General shall report its findings to the General Assembly no later than October 1, 2021.**

I. CURRENT PERMITTING REQUIREMENTS AND EXEMPTIONS

- **OCRP is responsible for permit review and approval.**
- **If an organization does not provide enough information for OCRP to make a decision, OCRP has authority to not issue a permit.**
- **All permit denials, suspensions and revocations are required to be approved by the Board.**
- **VDACS has not recommended a permit for denial in at least eight years.**

II. NET REVENUE DEDICATED TO CHARITABLE ACTIVITIES

- **Permitted organizations are required to report gross receipts to VDACS on a quarterly basis with an annual requirement to meet the use of proceeds.**
- **Receipts from electronic pull-tabs in an organization's private social quarters are not required to be included in an organization's gross receipts.**
- **Reports filed are subject to audit by OCRP.**
- **Use of proceeds is currently set to 10% by the Board.**

III. CHARITABLE GAMING OCCURRING IN REMOTE LOCATIONS NOT LOCATED IN THE SAME JURISDICTION

- **Effective July 1, 1996, charitable organizations were restricted in the location they were permitted to conduct charitable gaming.**
- **In 2006, the *Code of Virginia* was updated to only restrict charitable gaming locations for bingo and provided VDACS with the authority to approve exceptions.**
- **In 2020 the *Code of Virginia* was updated to remove the regional jurisdiction requirement.**

III. CHARITABLE GAMING OCCURRING IN REMOTE LOCATIONS NOT LOCATED IN THE SAME JURISDICTION

- In 2021 the *Code of Virginia* was updated to apply the same requirements for the conduct of bingo games. In accordance with the *Code of Virginia*, if the charitable organization was already conducting charitable gaming at a location “That, notwithstanding §§ 18.2-340.26:1, 18.2-340.27, 18.2-340.28, and 18.2-340.28:1 of the Code of Virginia, as amended by this act, any organization that conducted bingo, network bingo, instant bingo, pull tabs, or seal cards at a location outside of the county, city, or town in which its principal office, as registered with the State Corporation Commission, is located or an adjoining county, city, or town on or before February 1, 2021, may continue to conduct bingo, network bingo, instant bingo, pull tabs, or seal cards at such locations until June 30, 2022.”**

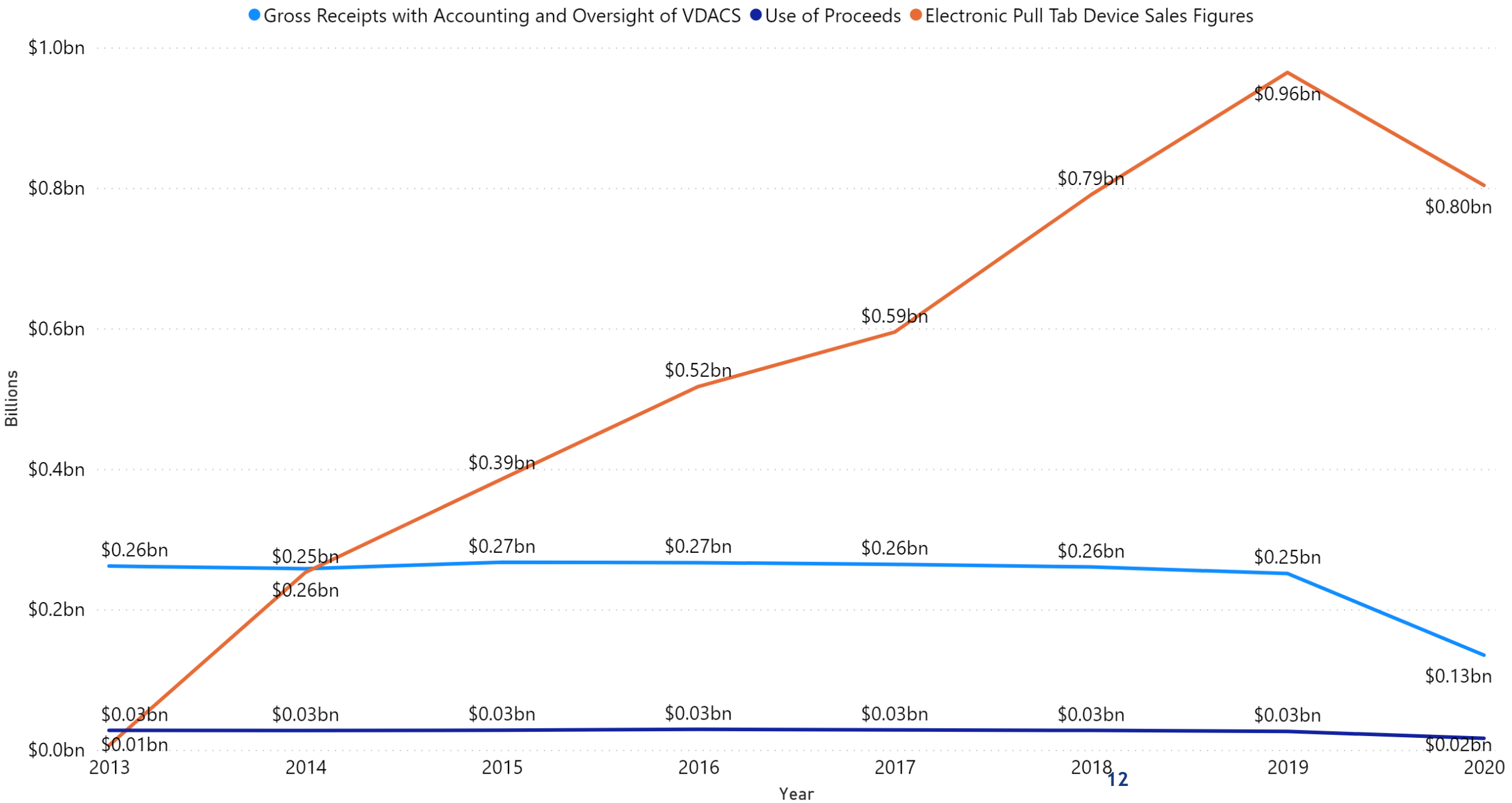
III. CHARITABLE GAMING OCCURRING IN REMOTE LOCATIONS NOT LOCATED IN THE SAME JURISDICTION

- In 2021 the *Code of Virginia* was updated to restrict the location for the sale of instant bingo, pull tabs, or seal cards within the organization's social quarters; with the exception of associations of war veterans or auxiliary units thereof organized in the United States or a fraternal association or corporation operating under the lodge system.**

IV. ENFORCEMENT OF SOCIAL QUARTERS AND MEMBERS AND GUESTS LIMITATIONS

- **Electronic pull tab devices comprise the majority of charitable gaming sales.**
- **As of August 2021, 92% of electronic pull tab devices were located in social quarters.**
- **VDACS does not authorize individual electronic handheld devices. VDACS verifies that charitable organizations have no more than 50.**
- **VDACS does permit electronic pull tab machines, but not the number, so once VDACS authorizes one, the permit is authorized for up to 18. That is VDACS' limit when it comes to authorizing.**

Select Charitable Gaming Figures by Year

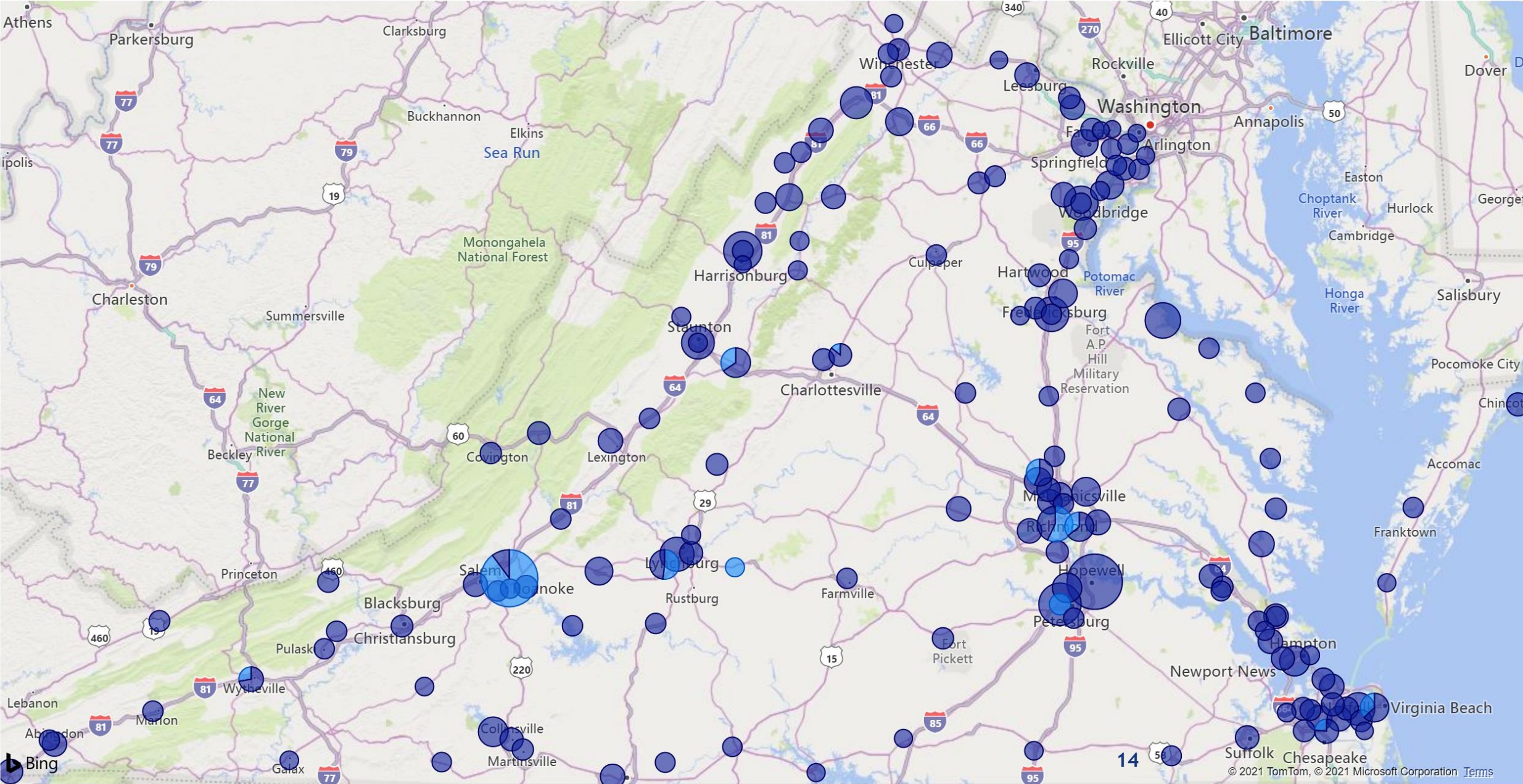


IV. ENFORCEMENT OF SOCIAL QUARTERS AND MEMBERS AND GUESTS LIMITATIONS

Year	Gross Receipts with Accounting and Oversight of VDACS	Use of Proceeds	Licensed Organizations	Electronic Pull Tab Device Sales Figures
2013	\$261.7	\$27.8	365	\$106.9
2014	\$258	\$27.6	359	\$252.7
2015	\$267.1	\$27.9	361	\$385.7
2016	\$266.5	\$29.3	347	\$517.8
2017	\$264.1	\$28.4	313	\$594.8
2018	\$260.4	\$27.7	294	\$790.3
2019	\$251.1	\$26.2	301	\$964.4
2020	\$134.9	\$16.5	273	\$803.8
Financial figures are in millions -- All numbers were provided by VDACS				

Total Devices by Zip Code and Bingo Hall/Social Quarters

Bingo Hall/Social Quarters ● Bingo Hall ● Social Quarters



VDACS OBSERVATION 1

The terms "members" and "guests" are undefined when related to a particular organization and the activities performed under Code §18.2-340.26:1.

VDACS OBSERVATION 2

The type of organization allowed to perform activities under Code § 18.2-340.26:1 does not align with IRS guidelines.

VDACS OBSERVATION 3

Private social quarters are not required to engage in other social recreational or fraternal activities in conjunction with charitable gaming activities.

VDACS OBSERVATION 4

Private social quarters are not required to operate in a facility where the organization regularly conducts business related to its federal tax-exempt purpose.

VDACS OBSERVATION 5

Organizations engaging in activities performed under Code § 18.2-340.26:1 are not subject to the reporting and auditing requirements under § 18.2-340.31.

V. THE STRUCTURE OF THE CHARITABLE GAMING BOARD INCLUDING ANY CHANGES NEEDED TO PREVENT CONFLICTS OF INTEREST

- **Six of the eleven board members have potential conflicts of interest due to *Code* requirements.**
- **Six represents a majority overall on the board and is one more than the five (45%) required for a quorum.**
- **In accordance with the *Code*, board members are required to recuse themselves from voting on matters where they or their immediate families have a personal or other interest.**

V. THE STRUCTURE OF THE CHARITABLE GAMING BOARD INCLUDING ANY CHANGES NEEDED TO PREVENT CONFLICTS OF INTEREST

- In accordance with Charitable Gaming Board bylaws, board members shall abstain or otherwise recuse themselves from voting on any matter in which they or a member of their immediate family have a personal or other interest in a transaction as defined in §2.2-3101 of the Code of Virginia.**

FINDING 1 - TEXAS HOLD'EM REGULATIONS CREATE ISSUES THAT IMPAIR THE INTEGRITY OF THE CHARITABLE GAMING PROGRAM

- **Regulations in their current form:**
 - **Allows for the transfer of management of Texas Hold'em from charitable organizations to third parties.**
 - **Specifically allows conflicts of interest between the landlord, the operator, and the members of the organizations.**
 - **Creates undue burden on VDACS oversight and enforcement due to the lack of consistency between bingo game and Texas Hold'em regulations.**

OSIG RECOMMENDATION 1

The General Assembly should consider updating the *Code of Virginia* to ensure that the management, operation, conduct and administration of charitable gaming is the responsibility of the permitted charitable organizations.

OSIG RECOMMENDATION 2

The General Assembly should consider updating the *Code of Virginia* to establish requirements that protect charitable gaming from conflicts of interests, improve oversight and enforcement, and provide consistency in charitable gaming requirements between bingo and Texas Hold'em poker tournaments.

OSIG RECOMMENDATION 3

The General Assembly should consider updating the *Code of Virginia* to establish limitations in expenses and remuneration that will also provide consistency across the charitable gaming program.

OSIG RECOMMENDATION 4

The General Assembly should consider updating the *Code of Virginia* to require licensing and regulation of the landlord, specifically a landlord that provides a leased location for two or more charitable organizations conducting charitable gaming on the landlord's premises.

FINDING 2 - A BOARD MEMBER DID NOT RECUSE THEMSELVES IN ACCORDANCE WITH CODE REQUIREMENTS

- **Board members are required to recuse themselves when they or an immediate family member have a personal or other interest in a transaction.**
- **A board member disclosed a potential personal interest in Texas Hold'em.**
- **Although the potential personal interest was disclosed, that Board member did not and has not recused themselves from participating in discussion, promulgation of regulations or voting related to their current interest.**

OSIG RECOMMENDATION 5

The General Assembly should change the Charitable Gaming Board to an advisory board to protect the integrity of the Commonwealth's charitable gaming oversight program.

FINDING 3 - VDACS MADE APPLICATIONS FOR TEXAS HOLD'EM POKER AVAILABLE PRIOR TO PUBLIC POSTING OF REGULATIONS

- **Code prohibits VDACS from denying permits without the review and approval of the board.**
- **VDACS made applications for Texas Hold'em permits available under the assumption that the regulations would be promulgated.**
- **After VDACS had done this, HB1800 Line Item 105 D2 prohibited the Charitable Gaming Board from promulgating new regulations.**

FINDING 3 - VDACS MADE APPLICATIONS FOR TEXAS HOLD'EM POKER AVAILABLE PRIOR TO PUBLIC POSTING OF REGULATIONS

- **VDACS could not issue permits due to regulations not being promulgated.**
- **A charitable organization sued because they applied for and were not issued a permit.**
- **This charitable organization is represented by one of the board members, and this creates a conflict with the current requirements for denying permits.**

OSIG RECOMMENDATION 6

- **VDACS should not make applications available for new charitable games or regulatory changes that require permit updates until a specified time frame after regulations have been promulgated.**
- **This would allow all interested charitable organizations time to assess the requirements of the new regulations.**

OSIG RECOMMENDATION 7

The General Assembly should consider updating the authority of VDACS to have responsibility for the requirements, qualifications and grounds for issuance of all types of licenses/permits required for charitable gaming, including authority to deny, suspend and revoke.

OSIG RECOMMENDATION 8

In the event recommendation #7 is not implemented, the General Assembly should consider updating the authority of VDACS to deny, suspend or revoke permits in situations where a Board member or their immediate family member is associated with the charitable organization.

FINDING 4 - VDACS LACKS STATUTORY AUTHORITY TO REGULATE LANDLORDS

- **VDACS lacks the statutory authority to regulate property owners that lease to organizations who conduct charitable gaming.**
- **The Code of Virginia places certain expectations on property owners in § 18.2–340.33.6, but gives VDACS no authority or resources to oversee and enforce these expectations.**
- **Other states (Colorado and Texas) recognize the potential for fraud and abuse in the lessor to lessee relationship in this area and the need to regulate the property owner component of charitable gaming as a result.**

OSIG RECOMMENDATION 9

The General Assembly should consider updating the *Code of Virginia* to require the licensing of the owner, lessor or lessee of premises where charitable gaming occurs.

CHANGES NEEDED TO PREVENT CONFLICTS OF INTEREST WITHIN THE CHARITABLE GAMING BOARD

- In order for the General Assembly to prevent conflicts of interests within the Charitable Gaming Board, it would need to require that Board members and their families have no direct or indirect financial interest in charitable gaming activities.
- This matches with the Code requirements for the Lottery Board ([§ 58.1-4004](#)) and the Virginia Racing Commission ([§ 59.1-368](#)). Virginia Lottery and the Virginia Racing Commission are the two other Commonwealth agencies responsible for the oversight of gambling activities.

CHANGES NEEDED TO PREVENT CONFLICTS OF INTEREST WITHIN THE CHARITABLE GAMING BOARD - ALTERNATIVE

Though it will not prevent conflicts of interest within the Board, establishing the Board as an advisory board may be an option the General Assembly should consider. OSIG recognizes that charitable gaming potentially benefits from the industry knowledge of the Board, but the powers of the Board do not align with a board with established conflicts.

CHANGES NEEDED TO PREVENT CONFLICTS OF INTEREST WITHIN THE CHARITABLE GAMING BOARD - ALTERNATIVE

OSIG recommends that the General Assembly consider establishing the Charitable Gaming Board as an advisory board and giving VDACS the authority to regulate charitable gaming. The makeup of the Board matches the definition of an advisory board in accordance with Code [§ 2.2-2100](#). This will reduce the impact of the conflicts of interest inherent within the Board makeup.

VI. THE ADEQUACY OF ENFORCEMENT AND RESOURCES DEDICATED TO OVERSIGHT ACTIVITIES OF THE OFFICE OF CHARITABLE AND REGULATORY PROGRAMS

- **VDACS' enforcement process is lengthy and can take years to work fully through the process, depending on the violation.**
- **VDACS lacks authority to revoke a license without Board approval, regardless of the reason for suspending or revoking a permit. This increases administrative burden on VDACS as they work with the organization to return to compliance without the ability to revoke or suspend.**

VI. THE ADEQUACY OF ENFORCEMENT AND RESOURCES DEDICATED TO OVERSIGHT ACTIVITIES OF THE OFFICE OF CHARITABLE AND REGULATORY PROGRAMS

- **VDACS does not have Oversight and Enforcement Authority for over 70% of charitable gaming gross receipts in the Commonwealth. This does not align with the intent of having state oversight of charitable gaming in the Commonwealth.**
- **Currently, six of VDACS' fourteen positions dedicated to charitable gaming are vacant. Changes to the program will impact staffing needs to meet proper oversight and enforcement requirements.**

FINDING 5 - VDACS DOES NOT HAVE THE SUFFICIENT STAFFING TO MEET THEIR OVERSIGHT AND ENFORCEMENT REQUIREMENTS

- **VDACS does not have the staffing necessary to meet their oversight and enforcement requirements.**
- **As of September 15, 2021, VDACS has six of their fourteen positions dedicated to charitable gaming vacant.**
- **The audit, financial review, and inspection processes are key in ensuring charitable gaming activities are conducted appropriately and in compliance with applicable regulations.**
- **Without sufficient resources dedicated to oversight and enforcement activities, there is an increased risk for fraud, operational inefficiencies, and overall negative impacts to the credibility of charitable gaming within the Commonwealth.**

OSIG RECOMMENDATION 10

VDACS should perform an assessment of charitable gaming staffing resources to determine the gap between the number of authorized positions and the number and types of positions needed to fulfill statutory and regulatory missions, and VDACS should recruit accordingly.

OSIG RECOMMENDATION 11

VDACS charitable gaming needs to have the resources available to not only complete the assigned oversight and enforcement responsibilities, but the resources available to follow up on outstanding items and revisit charitable organizations that continue to not comply with regulations, and escalate and improve the revocation process timeline.

FINDING 6 - VDACS DOES NOT HAVE OVERSIGHT OF MORE THAN 70% OF CHARITABLE GAMING GROSS RECEIPTS

Year	Bingo Electronic Pull Tab Machine Ticket Sales	Social Quarter Electronic Pull Tab Machine Ticket Sales
2018	\$20,725,276.55	\$285,740,736.60
2019	\$17,320,909.35	\$338,838,391.40
2020	\$6,852,525.15	\$329,749,550.44

- Data shown is reported from one device manufacturer who, per VDACS data, had 133 machines in bingo halls and 813 machines in social quarters as of August 2021.**

FINDING 6 - VDACS DOES NOT HAVE OVERSIGHT OF MORE THAN 70% OF CHARITABLE GAMING GROSS RECEIPTS

- In August 2021, 2,234 (92%) of electronic pull tab devices were located within social quarters where gross receipts aren't included in reporting and VDACS has no oversight and accounting.**
- Based on sales figures provided from VDACS and electronic pull tab device manufacturers, OSIG identified OCRP as having oversight and enforcement of less than 27% of charitable gaming gross receipts occurring in the Commonwealth in 2019 and less than 17% in 2020.**

OSIG RECOMMENDATION 12

- **The General Assembly should consider updating the *Code of Virginia* to include gross receipts from electronic pull tab machines under VDACS's authority and oversight as intended by the General Assembly when establishing the program and vesting the agency with control of all charitable gaming in the Commonwealth.**
- **OSIG also recommends that VDACS identify the resources necessary to effectively implement its authority and perform oversight of charitable gaming in the Commonwealth.**

FINDING 7 - LENGTHY REVOCATION PROCESS FOR CHARITABLE GAMING PERMITS

- **The process to deny, suspend or revoke a permit can take years depending on the type of violation.**
- **Organizations cannot have their permit revoked for failing to meet use of proceeds without an opportunity to implement a remedial business plan.**
- **The board has final approval on denying, suspending or revoking permits instead of OCRP.**
- **The process ending with the board leaves revocation open to actual or the appearance of conflicts of interest of board members.**

OSIG RECOMMENDATION 13

The *Code of Virginia* should be updated to give VDACS the authority to suspend or revoke permits instead of the Board. This is in line with OSIG's other recommendations to change the Board from a policy to an advisory board. OSIG also recommends that VDACS management work to shorten the length of time that suspending or revoking permits take in response to any *Code* changes.

OVERALL ADEQUACY OF ENFORCEMENT AND RESOURCES DEDICATED TO OVERSIGHT ACTIVITIES

- **VDACS does not have oversight and enforcement authority for more than 70% of charitable gaming gross receipts in the Commonwealth. The actual percentage is higher than OSIG's estimate.**
- **OSIG took a conservative approach to provide a quantifiable estimate to provide to the General Assembly. This does not align with the intent of having state oversight of charitable gaming in the Commonwealth.**

OVERALL ADEQUACY OF ENFORCEMENT AND RESOURCES DEDICATED TO OVERSIGHT ACTIVITIES

Six of VDACS 14 positions dedicated to charitable gaming are vacant. Changes to the program, including OSIG's recommended oversight of all charitable gaming funds and the implementation of Texas Hold'em poker tournaments, will affect staffing needs to meet proper oversight and enforcement requirements.

OVERALL ADEQUACY OF ENFORCEMENT AND RESOURCES DEDICATED TO OVERSIGHT ACTIVITIES

- **It is OSIG's opinion that charitable gaming would not be more appropriately vested under the Virginia Lottery, and that the cons of moving regulation of charitable gaming under Lottery outweigh the pros.**

REGULATING AUTHORITY FOR CHARITABLE GAMING

OSIG recommends that charitable gaming remain with the Virginia Department of Agriculture and Consumer Services. The General Assembly should change the Charitable Gaming Board from a policy board to an advisory board. In doing so, the General Assembly should also transfer authority for regulating charitable gaming from the Board to the Office of Charitable and Regulatory Programs under VDACS.

CONSIDERATIONS FOR A SINGLE GAMING AGENCY

- Lottery is in the middle of standing up casinos and sports betting.
- Each gaming industry and their regulations are nuanced and combining gaming under a single agency could cause certain aspects of gaming to get overlooked.
- Lottery and the Racing Commission already have conflicts of interest requirements in *Code*.
- Currently, three boards are involved with gaming in the Commonwealth.
- Other states have gaming regulation split between agencies. Massachusetts splits gaming regulation between their Lottery and their Attorney General.

OTHER STATES WITHOUT BOARD REGULATION OF CHARITABLE GAMING

- **Kansas – Department of Revenue**
- **Louisiana – Department of Revenue**
- **Massachusetts – State Lottery**
- **Michigan – Lottery**
- **North Dakota – Attorney General**
- **Ohio – Attorney General**
- **West Virginia – Department of Revenue**

PROS OF MOVING CHARITABLE GAMING TO LOTTERY

- **Lottery already performs inspections.**
- **The Lottery Board has conflicts of interest requirements built into Code.**
- **There would be fewer agencies regulating gaming.**
- **Lottery's status as an independent agency allows for greater flexibility than OCRP currently has.**

CONS OF MOVING CHARITABLE GAMING TO LOTTERY

- **Charitable gaming is already established under VDACS. Moving it could be problematic and create confusion amongst the industry, staff and charities.**
- **Lottery, and it's Board, is standing up significant new regulatory responsibilities and does not have an existing knowledge base to take over charitable gaming.**

CONS OF MOVING CHARITABLE GAMING TO LOTTERY

- **The General Assembly and/or Lottery would need to resolve the existence of both the Lottery Board and the Charitable Gaming Board.**
- **The Lottery Board already has two new members new to the gaming industry, and adding more members or another board could negatively impact operations.**

WHETHER CHARITABLE GAMING PROGRAM SHOULD MOVE TO LOTTERY

OSIG recommends that Charitable Gaming remain with the Virginia Department of Agriculture and Consumer Services. The General Assembly should change the Charitable Gaming Board from a policy board to an advisory board, similar to Virginia Lottery. In doing so, the General Assembly should also transfer authority for regulating charitable gaming from the Board to the Office of Charitable and Regulatory Programs under VDACS.

TAKEAWAYS

- **OCRP needs additional resources and authority to enforce charitable gaming.**
- **The Board has conflicts of interest prohibited in other gambling boards.**
- **Changing the Board from a policy board to an advisory board would potentially negate conflicts of interest.**
- **OCRP should have the ability to deny, suspend or revoke permits without Board involvement.**