

Department of Legislative Services
 Maryland General Assembly
 2007 Special Session

FISCAL AND POLICY NOTE

House Bill 41 (Delegate Riley)
 Ways and Means

Gaming - Video Lottery Terminals and Slot Machines

This bill authorizes up to 15,500 video lottery terminals (VLTs) at seven locations – four horse racing tracks and three unspecified nontrack locations; provides for one-time application fees; provides for the distribution of VLT proceeds; creates the Education Trust Fund (ETF) and other special funds; mandates funding for the Geographic Cost of Education Index (GCEI) and K-12 and higher education capital projects; and continues the current prohibition on additional forms of commercial gambling.

The bill takes effect June 1, 2008.

Fiscal Summary

State Effect: Special fund revenues increase in FY 2011 and beyond due to one-time license fees and VLT revenues. General fund revenues decrease beginning in FY 2011 due to decreased lottery sales; future year losses increase with VLT implementation, totaling \$85.3 million in FY 2013. General fund expenditures decrease in FY 2009 due to one-time license fee revenues, offset by increases due to lottery start-up costs. General fund expenditures increase in FY 2010 and beyond due to mandated GCEI funding and other State agency expenditures, offset by a decrease in general fund expenditures beginning in FY 2012 due to the availability of ETF revenues. Special fund revenues and expenditures increase for the purposes specified in the bill beginning in FY 2011. Special fund expenditures for education begin in FY 2011. **Appendix 1** shows the revenues and expenditures by fund in greater detail.

(in dollars)	FY 2009	FY 2010	FY 2011	FY 2012	FY 2013
GF Revenue	\$0	\$0	(\$23,944,453)	(\$73,823,906)	(\$85,260,000)
SF Revenue	93,000,000	0	262,800,098	800,657,568	901,759,693
GF Expenditure	(79,250,000)	58,222,068	28,884,043	(370,426,572)	(432,208,847)
SF Expenditure	93,000,000	50,000	262,850,098	800,657,568	901,759,693
Net Effect	\$79,250,000	(\$58,272,068)	(\$52,878,496)	\$296,602,665	\$346,948,847

Note: () = decrease; GF = general funds; FF = federal funds; SF = special funds; - = indeterminate effect

Local Effect: Revenues for localities with VLT facilities would increase by approximately \$19.8 million in FY 2011, increasing to \$57.5 million in FY 2013. Local expenditures increase significantly for local governments with VLT facilities.

Small Business Effect: Meaningful.

Analysis

Bill Summary: The major provisions of the bill are as follows:

Oversight	<p>Nine member State Lottery Commission.</p> <p>Addition of four members to existing five-member commission.</p> <p>One member of Racing Commission appointed as liaison to State Lottery Commission and vice versa.</p> <p>Commission provides and operates a single central computer.</p>
Selection of Location	<p>Establishes a nine-member Video Lottery Facility Location Commission.</p> <p>Awards up to seven operation licenses through competitive bid. As many as four licenses may be awarded to racetrack locations; up to three licenses may be awarded to nonracetrack locations.</p> <p>No more than two licenses may be awarded in any county.</p>
Number of VLTs	<p>Authorizes up to 15,500 video lottery terminals (VLTs).</p> <p>State Lottery Commission may redistribute unallocated terminals to maximize revenue.</p> <p>Maximum of 7,500 VLTs in a single county.</p> <p>Maximum of 5,000 VLTs under a single license.</p> <p>Maximum of 6,000 VLTs allocated to a single business entity.</p>

Award Criteria	<p>Proposals evaluated based on:</p> <ul style="list-style-type: none"> • 70% business and market factors; • 15% economic development; and • 15% location siting factors.
Restrictions on Ownership	<p>License holders may not hold licenses for racetrack and nonracetrack locations.</p> <p>Interest not allowed in more than two racetrack locations or one nonracetrack location.</p>
Term of License	<p>15-year initial term, with a 10-year renewal period.</p> <p>Operations must begin within 18 months of issuance of a license, with extensions available.</p> <p>Operations at racetrack locations must be fully operational at a permanent facility within two years.</p>
Application Fees	<p>Application fees of \$3 million per 500 VLTs accrue to the Education Trust Fund.</p>
Capital Investment	<p>An applicant must provide a \$15 million prorated capital investment per 500 VLTs, with ongoing investment of \$1 million per 1,000 VLTs for capital maintenance.</p>
Racing Days	<p>A racetrack location awarded an operations license must maintain at least as many live racing days as were authorized for that location in 2005.</p>
Racing Events	<p>Licenses issued for the Pimlico Race Course or Laurel Park will be revoked if the Preakness Stakes or Woodlawn Vase are transferred to a location outside the State.</p> <p>The licensee must allow the Maryland Million to be run annually at Laurel Park, barring unforeseen circumstances.</p>

Contracting and Hiring	Construction must meet minority business enterprise requirements, with preferences in employee hiring offered to local residents.
Payout	Average annual payout of 90%, with authority to increase the percentage to 95% by regulation.
Distribution of Proceeds	<p>5% to counties for local development grants, with amount divided based on facility proceeds.</p> <p>5.1% to the Purse Dedication Account in the first year, and 5.8% in subsequent years.</p> <p>5% to the State Lottery Agency for administration in the first year, and 4.3% in subsequent years. Any excess funds are equally divided between the Education Trust Fund and the Purse Dedication Account.</p> <p>Gross proceeds may not exceed 30% at nonracetrack locations and 36% at racetrack locations.</p> <p>Remainder to Education Trust Fund.</p>
Purse Dedication Fund	<p>Amount available to thoroughbred and standardbred industries based on the total percentage of total wagering on that industry at State racetracks in the prior year.</p> <p>89% of the proceeds available to each industry will benefit purses, with the remainder available to the industry's race fund.</p> <p>\$125,000 may be directed to each of two horsemen's assistance funds to provide health benefits.</p>
Education Trust Fund	<p>Provides funds for education of children in prekindergarten through grade 12 through Bridge to Excellence in Public Schools. Mandates funding of the GCEI phased in from fiscal 2010 to 2012.</p> <p>Requires the Governor to provide at least \$150 million annually in fiscal 2010-2020 K-16 public school construction and improvements.</p> <p>Provides funds to increase undergraduate student financial aid.</p>

Terminal Fees	\$390 per terminal per year, payable to the Compulsive Gambling Fund in the Department of Health and Mental Hygiene (DHMH). 15,500 terminals would generate \$6.0 million per year.
Prevalence Study	DHMH must conduct study of prevalence of problem gambling.
State Lottery Games	May not be offered for sale at a video lottery facility.
Other Provisions	Expands limited slot machine operations by fraternal, religious, veterans' organizations, and affiliated nonprofits to all counties in the State.
	<i>May also choose to include food and drink, restrictions to entry, exclusions, consumer protections</i>

Current Law: Specified types of gambling are allowed in Maryland. This includes the State lottery and wagering on horse racing. Bingo, bazaars, and gaming nights are allowed for some nonprofit organizations on a county-by-county basis. Several counties permit for-profit bingo. In addition, some nonprofit organizations in Eastern Shore counties are allowed to operate up to five slot machines, provided that at least 50% of the proceeds go to charity. VLTs are not authorized for operation in the State. For more information on gambling and horse racing in Maryland, consult the *Legislators' Guide to Video Lottery Terminal Gambling*.

State Revenues:

Application Fee Revenues

The bill requires licensees to pay an application fee of \$3 million for each 500 VLTs awarded. Application fees must be paid by October 1, 2008. These fees are to be distributed to the ETF. Assuming that the commission awards all of the VLTs and licensees opt to participate and pay their license fee by the required deadline, special fund revenues would increase by \$93 million in fiscal 2009.

VLT Revenues

Seven locations in the State may be licensed to operate a total of 15,500 VLTs. Four VLT facilities must be located at horse racing tracks and three VLT facilities must be located at three nontrack locations to be determined by the Location Commission.

As a result, total revenues generated – after payouts to winning players, but **before** any other distributions are made – could total approximately \$33.6 million in fiscal 2009, \$814.6 million in fiscal 2010, \$1.54 billion in fiscal 2011, and approximately \$1.61 billion in fiscal 2012 and later.

Since the bill does not specify locations for VLT facilities, the WPD estimate is based on a statewide average WPD developed from an independent analysis of the market for VLTs in Maryland by the Department of Legislative Services (DLS). The market analysis includes the impact of recent VLT expansions in Delaware and West Virginia, the opening of VLT facilities in Pennsylvania, and the proximity of proposed Maryland locations to other VLT facilities and population centers. Legislative Services advises that gross VLT revenue estimates could be higher or lower than estimated depending on the actual locations awarded VLT licenses and the economic and market conditions that develop as the bill is implemented, including expansion of gaming in the surrounding states.

Exhibit 1 details many of the important assumptions in these estimates.

Exhibit 1 Assumed Status of Operation and Win-per-day (WPD)

<u>Location</u>	<u>Allocation</u>	<u>WPD</u>	<u>Begin Operations</u>	<u>Full Capacity</u>
Horse Tracks	7,750	\$236	October 2010	October 2011
Nontracks	7,750	236	April 2011	April 2012

Other Assumptions

- VLTs will operate 365 days a year, once operational.
- Virginia and Washington, DC do not authorize VLT gambling.
- West Virginia and Delaware do not expand VLT operations, either by adding additional VLT facilities or authorizing casino-style gambling.

- Pennsylvania does not expand gambling beyond VLT facilities authorized in 2004.

Distribution of Revenues

Exhibit 2 details the revenue distribution resulting from VLTs for fiscal 2010 through 2013.

Exhibit 2				
Distribution of VLT Revenues				
(\$ in Millions)				
	<u>FY 2010</u>	<u>FY 2011</u>	<u>FY 2012</u>	<u>FY 2013</u>
Total Annual Gross	\$0.0	\$396.9	\$1,190.7	\$1,336.9
ETF (54.9%/48.9%)	\$0.0	\$199.1	\$614.8	\$693.8
Licensees (30%/36%)	\$0.0	\$137.9	\$396.1	\$441.2
PDA (5.1%/5.8%)	\$0.0	\$20.2	\$65.7	\$77.5
Local (5%)	\$0.0	\$19.8	\$54.5	\$57.5
Lottery Operations (5%/4.3%)	\$0.0	\$19.8	\$59.5	\$66.8

Effect on Lottery Sales

Legislative Services estimates that VLTs, when fully implemented, will cause a permanent reduction in lottery revenues of 10% annually versus what is currently forecasted. This estimate is based on the experience of other states that have authorized additional gambling and experienced substantial decreases in lottery sales. In addition, for those states where data are available, Maryland has substantially greater lottery operations, measured on both a gross volume and per capita basis. Therefore, it is possible that lottery sales might decrease more sharply than these other states. **Exhibit 3** details the estimated decline in general fund revenue in each fiscal year as a result of decreased lottery sales. The impact on lottery revenues incorporates current lottery revenue forecasts and increases with increased VLT implementation.

Exhibit 3
Estimated Loss in General Fund Revenue
Due to Decreased State Lottery Sales
(\$ in Millions)

<u>FY 2010</u>	<u>FY 2011</u>	<u>FY 2012</u>	<u>FY 2013</u>
\$0	\$23.9	\$73.8	\$85.3

The Lottery Agency estimates that lottery revenues would decline by 1% in fiscal 2009, 5% in fiscal 2010, 3% in fiscal 2011, and 1% in fiscal 2012 before rebounding in fiscal 2013 and beyond.

State Expenditures: Mandated expenditures would increase by an estimated \$68.4 million in fiscal 2010, the first year of the three-year phase-in proposed in the bill. This amount would increase to \$104.5 million in fiscal 2011 and \$142.2 million in fiscal 2012.

Consistent with the Administration's stated intent to fund a three-year phase-in of the GCEI formula beginning in fiscal 2009, DLS estimates of State aid for the GCEI formula assume that a phase-in of the formula will begin in fiscal 2009 (at 30%) and will be complete by fiscal 2011. Relative to DLS estimates, the GCEI phase-in established in the bill would reduce general fund expenditures by an estimated \$40.1 million in fiscal 2009, by \$13.7 million in fiscal 2010, and by \$34.8 million in fiscal 2011. There would be no savings to the State after fiscal 2011 because the GCEI formula would be fully phased in by fiscal 2012.

Additional Information

Prior Introductions: Over the past several legislative sessions, various proposals have been introduced to authorize VLTs at the State's horse racing tracks or other destinations in the State. In 2005, separate legislation was passed by the Senate and House of Delegates, but differences in the bills were never reconciled.

Cross File: None.

Information Source(s): City of Laurel; Allegany County; Prince George's County; Howard County; Maryland State Lottery Agency; Department of State Police; Anne

Arundel County; Department of Health and Mental Hygiene; Maryland Department of Transportation; Department of Labor, Licensing, and Regulation, Department of Budget and Management; Department of Public Safety and Correctional Services; Baltimore City; Maryland State Department of Education; Office of the Attorney General; Innovation Group; State Department of Assessments and Taxation; Department of Legislative Services

Fiscal Note History: First Reader - November 2, 2007
mcp/rhh

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Appendix 1

	<u>FY 2009</u>	<u>FY 2010</u>	<u>FY 2011</u>	<u>FY 2012</u>	<u>FY 2013</u>
Gross VLT Revenues	\$0	\$0	\$396,888,507	\$1,190,665,520	\$1,336,887,601
Licensees	\$0	\$0	\$137,866,534	\$396,052,952	\$441,172,908
Special Fund Revenues					
Education Trust Fund	\$0	\$0	\$199,091,808	\$614,822,075	\$693,844,665
Purse Dedication Account	0	0	20,241,314	65,744,233	77,539,481
Compulsive Gambling	0	0	3,778,125	6,045,000	6,045,000
Local Distributions	0	0	19,844,425	54,512,985	57,486,167
Lottery VLT Administrative	0	0	19,844,425	59,533,276	66,844,380
License Fees – to ETF	93,000,000				
Total SF Revenues	\$93,000,000	\$0	\$262,800,098	\$800,657,568	\$901,759,693
GF Revenues					
Lost Lottery Revenue	\$0	\$0	(\$23,944,453)	(\$73,823,906)	(\$85,260,000)
Total GF Revenues	\$0	\$0	(\$23,944,453)	(\$73,823,906)	(\$85,260,000)
Special Fund Expenditures					
Education Trust Fund	\$93,000,000	\$0	\$199,091,808	\$614,822,075	\$693,844,665
Purse Dedication Account	0	0	20,241,314	65,744,233	77,539,481
Compulsive Gambling	0	0	3,778,125	6,045,000	6,045,000
Local Distributions	0	0	19,844,425	54,512,985	57,486,167
Lottery VLT Administrative	-	0	19,844,425	59,533,276	66,844,380
Transportation – Studies	-	50,000	50,000		
Total SF Expenditure	\$93,000,000	\$50,000	\$262,850,098	\$800,657,568	\$901,759,693
GF Expenditures					
DBM – Consultant	\$250,000				
Attorney General	0	\$259,611	\$273,972	\$289,282	\$305,619
State Police		639,427	462,783	472,451	599,293
GCEI	0	57,323,030	77,239,096	93,633,770	110,730,906
DHMH - Prevalence Study	500,000				
Lottery – Start-up costs	13,000,000				
Education – from ETF	(93,000,000)	0	(49,091,808)	(464,822,075)	(543,844,665)
MBE Studies		50,000		\$50,000	
Total GF Expenditures	(\$79,250,000)	\$58,222,068	\$28,884,043	(\$370,426,572)	(\$432,208,847)
Net Effect	\$79,250,000	(\$58,272,068)	(\$52,878,496)	\$296,602,665	\$346,948,847