

Department of Legislative Services
2010 Session

FISCAL AND POLICY NOTE

House Bill 512
Ways and Means

(Delegate Bromwell, *et al.*)

Video Lottery Terminals - Baltimore-Washington International Thurgood Marshall Airport

This bill authorizes a video lottery operation license to be awarded for a maximum of 2,500 video lottery terminals (VLTs) at the terminal building and surrounding area within the security perimeter of Baltimore-Washington International Thurgood Marshall Airport (BWI). The bill provides that for VLT proceeds from the BWI facility alone, the portion remaining after other distributions will be distributed to the Transportation Trust Fund (TTF) rather than to the Education Trust Fund.

The bill is contingent on the passage of House Bill 513, a constitutional amendment authorizing VLT gaming at BWI, and its ratification by voters in November 2010.

Fiscal Summary

State Effect: Special fund revenues increase in FY 2012 due to one-time license fees and beginning in FY 2014 due to VLT revenues from up to 1,000 VLTs. General fund expenditures increase in FY 2014 and beyond due to lottery agency expenditures. TTF revenues increase beginning in 2014. Special fund revenues and expenditures increase for the purposes specified by the VLT program beginning in FY 2014. Special fund expenditures for education occur in FY 2012 offsetting general fund expenditures of a like amount.

(in dollars)	FY 2011	FY 2012	FY 2013	FY 2014	FY 2015
SF Revenue	\$0	\$6,000,000	\$0	\$5,418,000	\$37,070,300
GF Expenditure	\$0	(\$6,000,000)	\$0	\$429,100	\$2,762,100
SF Expenditure	\$0	\$6,000,000	\$0	\$2,790,300	\$19,091,200
Net Effect	\$0	\$6,000,000	\$0	\$2,198,600	\$15,217,000

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

Local Effect: Revenues for local jurisdictions with VLT facilities will increase by approximately \$244,000 in FY 2014, increasing to \$2.0 million in FY 2015. Anne Arundel County infrastructure costs may increase depending upon specific plans for the site.

Small Business Effect: Small businesses will benefit from increased funds to the business investment account and to horse industry investments. Additional benefits from any construction and operation of VLT facilities will be partially offset by the substitution of VLT wagering for other expenditures.

Analysis

Bill Summary: The bill excludes a license at BWI from the prohibition against awarding more than one video lottery operation license in a single county or Baltimore City. The bill increases the limit on the number of VLTs in the State from 15,000 to 17,500, limits the number of VLTs that may be awarded for operation at BWI to 2,500, and increases the statewide limit on the number of VLT facilities from five to six. The bill requires that a bid for a video lottery operation license at BWI be submitted by April 15, 2012, and include the required initial license fee (\$3 million) and capital investment (\$25 million) for each 500 VLTs proposed in a bid.

Current Law: Chapter 5 of the 2007 special session, a constitutional amendment authorizing 15,000 VLTs at five locations in the State, was approved by Maryland voters at the November 2008 general election. The amendment also specifies that the General Assembly may only authorize expanded forms of gambling subject to certain restrictions. Chapter 4 of the 2007 special session establishes the operational and regulatory framework for the authorized VLT program.

A seven-member Video Lottery Facility Location Commission (Location Commission) established under Chapter 4 awards the video lottery operation licenses. Three members (including the chair) are appointed by the Governor, two each are appointed by the Senate President and the Speaker of the House of Delegates. Members may not be elected officials and must file annual financial disclosure statements.

The nine-member State Lottery Commission provides oversight for VLT implementation in the State. The State Lottery Commission owns and leases VLTs and the central monitor and control system. No elected officials may be appointed to the commission and a member of the commission serves as a liaison to the Racing Commission and vice versa.

Gross VLT proceeds are distributed as follows, pursuant to Chapter 4 of the 2007 special session:

- Business Investment – 1.5% to a small, minority, and woman-owned business investment account;
- Lottery (Administration) – 2% to the State lottery for administrative costs, with other costs provided for in the State budget;
- Local Government Impact Grants – 5.5% to local governments in which a video lottery facility is operating, 18% of which would go for 15 years (starting in fiscal 2012 and ending in fiscal 2027) to Baltimore City through the Pimlico Community Development Authority and to Prince George’s County for the community surrounding Rosecroft (\$1 million annually);
- Horse Racing Industry – 7% to a purse dedication account to enhance horse racing purses and funds for the horse breeding industry, not to exceed \$100 million annually;
- Racetrack Renewal – 2.5% for an eight-year period to a Racetrack Renewal Fund, not to exceed \$40 million annually;
- Licensee (Operator) – no more than 33% to video lottery operation licensees; and
- Education Trust Fund (ETF) – remainder to Education Trust Fund (48.5%-51.0%).

Education Funding

The Bridge to Excellence in Public Schools Act of 2002 (Chapter 288) altered the State’s school finance structure to align with a concept of “adequate funding” and phased in the enhanced State funding for public education over a six-year period. The legislation included a new program to adjust State aid to reflect regional cost differences. The Maryland State Department of Education oversaw the development of an acceptable Geographic Cost of Education Index (GCEI) to adjust State aid beginning in fiscal 2005. However, the Attorney General’s Office determined that funding for GCEI was not mandated in the Thornton bill. A GCEI was subsequently codified in the Budget Reconciliation and Financing Act (BRFA) of 2004 (Chapter 440); however, the 2004 BRFA did not mandate funding for the index.

ETF established by Chapter 4 of the 2007 special session provides funding for continuation of the Bridge to Excellence Act formulas and programs including GCEI funding. Public school construction and capital projects at public institutions of higher education, including community colleges, are also eligible for funding.

Transportation Trust Fund

TTF is a nonlapsing special fund that provides funding for transportation. It consists of tax and fee revenues, operating revenues (*e.g.*, transit fares, port fees, airport fees), bond proceeds, and fund transfers. The Maryland Department of Transportation (MDOT) issues bonds backed by TTF revenues and invests the TTF fund balance to generate investment income. The tax and fee revenues include motor fuel taxes, rental car sales taxes, titling taxes, vehicle registration fees, a portion of the corporate income and sales taxes, and other miscellaneous motor vehicle fees.

Video Lottery Terminals and Facilities

A maximum of 15,000 VLTs are authorized in the State, as follows:

- 4,750 VLTs at a location in Anne Arundel County within two miles of Route 295;
- 3,750 VLTs in Baltimore City, in a nonresidential area within one-half mile of Interstate 95 and Route 295, on city-owned land that is not adjacent to or within one-quarter mile of residential property;
- 2,500 VLTs at a location in Worcester County within one mile of the intersection of Route 50 and Route 589;
- 2,500 VLTs at a location in Cecil County within two miles of Interstate 95; and
- 1,500 VLTs on State property in Allegany County associated with the Rocky Gap State Park in a building physically separate from the Rocky Gap Lodge and Golf Resort.

VLT facilities must comply with all applicable planning and zoning laws of the local jurisdiction. The Location Commission may alter allocations if warranted by an evaluation of market and other factors; however, no more than 4,750 VLTs may be placed at any one location, and no more than one video lottery operating license may be awarded in a single county or Baltimore City. The commission is to evaluate bids based on: 70% on business and market factors, including the highest potential benefit to the State and percentage of Minority Business Enterprise (MBE) equity ownership; 15% on economic development factors; and 15% on location siting factors. There is no requirement for all five video lottery operation licenses to be issued.

Video Lottery Operation Licensing and Licensees

An individual or business entity may not own an interest in more than one video lottery facility. An initial license fee of at least \$3 million for every 500 VLTs is required, which accrues to ETF. The initial term of a video lottery operation license (of which up

to five may be awarded through a competitive bidding process) is 15 years; a licensee may subsequently reapply for an additional 10-year term.

License applicants must meet State MBE requirements for construction/procurement contracts and to the extent possible meet county MBE requirements if they exceed the State requirement. These requirements sunset on July 1, 2011. License applicants must also invest \$25 million in construction and related costs for every 500 VLTs proposed in a bid. VLT licensees must begin operations in a permanent facility within 18 months after the license is issued, which may be extended 6 months by the State Lottery Commission. VLT licensees must pay an annual fee of \$425 per VLT for a Problem Gambling Fund administered by the Department of Health and Mental Hygiene (DHMH). DHMH is required to conduct a problem and pathological gambling prevalence study to measure the rate of problem and pathological gambling in the State.

Other Provisions of Current Law

VLTs must have an average payout percentage of at least 87%. Free food and alcoholic beverages are generally prohibited at VLT facilities. By regulation, the State Lottery Commission must establish a list of individuals who are mandatorily excluded from VLT facilities. VLT facilities must develop procedures that permit self-exclusion from facilities for individuals with gambling problems. Regulations are also required for the protection of consumers, including a prohibition on cashing of paychecks at VLT facilities. A VLT facility may offer any State lottery game.

Background: The Location Commission has awarded three video lottery operation licenses to date. PPE Casino Resorts Maryland, LLC (PPE Casino Resorts) was awarded a license to operate a 4,750 VLT facility in Hanover in Anne Arundel County, contingent upon local zoning approval. Anne Arundel County Council approved favorable zoning legislation on December 21, 2009, which the county executive signed into law on December 22, 2009. The law has not gone into effect pending certification of a petition to require local voter approval of the law at the November 2010 election. PPE Casino Resorts expects to open a permanent facility adjacent to Arundel Mills Mall with 4,750 VLTs in December 2011.

Penn Cecil Maryland, Inc. (Penn Cecil) was awarded a license to operate a facility with 1,500 VLTs in Perryville in Cecil County. Penn Cecil is currently on schedule to open a permanent facility with 1,500 VLTs in October 2010.

Ocean Enterprise 589 LLC (OE 589) was awarded a license to operate a facility with 800 VLTs at Ocean Downs Racetrack in Worcester County. The facility is currently scheduled to open in fall 2010 with 600 VLTs, with the full complement of 800 VLTs in place by April 2011.

In February 2009, the Location Commission rejected a proposal for Allegany County that failed to meet the minimum requirements, including failing to pay the required license fee. In December 2009, the commission rejected the proposal for Baltimore City, finding that the proposal was not in the best interest of the State for a number of reasons. A protest of the commission's decision is pending before the Board of Contract Appeals. The Location Commission plans to rebid the Allegany County and Baltimore City (following resolution of the appeal) locations in 2010.

Projected revenues from the VLT operations under current law are shown in **Exhibit 1**.

Exhibit 1
Gross VLT Revenue Projections
(\$ in Millions)

	<u>FY 2011</u>	<u>FY 2012</u>	<u>FY 2013</u>	<u>FY 2014</u>	<u>FY 2015</u>
Education Trust Fund	\$60.0	\$144.9	\$372.4	\$479.1	\$523.2
Licensees	40.8	98.6	253.4	326.0	356.0
Local Government	6.8	16.4	42.2	54.3	59.3
Small, Minority, Woman-owned Businesses	1.9	4.5	11.5	14.8	16.2
Purse Dedication Account	8.7	20.9	53.7	69.1	75.5
Racetrack Renewal Account	3.1	7.5	19.2	24.7	27.0
Lottery Operations	<u>2.5</u>	<u>6.0</u>	<u>15.4</u>	<u>19.8</u>	<u>21.6</u>
Total Annual Gross	\$123.8	\$298.8	\$767.8	\$987.8	\$1,078.8

Source: Department of Legislative Services

BWI serves approximately 20 million commercial passengers annually. An estimated 72% (or 14.4 million) are age 21 or over. A Metropolitan Washington Council of Governments passenger survey indicates that more than half of passengers departing from Washington-Baltimore regional airports are not residents of the region. The Maryland Aviation Authority (MAA) assumes that the space within the security perimeter is the area past screening in the terminal building, beyond which only ticketed passengers and employees are allowed access.

Legislative Services is aware of two airports in the United States with VLTs, both in Nevada. McCarran International Airport contains about 1,270 slot machines and Reno-Tahoe International Airport has about 250 machines.

State Revenues: MAA advises that it currently has little space for VLTs within the security perimeter within the terminal building at BWI. Legislative Services assumes, based on the number of machines at the two airports in Nevada, that BWI could accommodate a maximum of 1,000 VLTs at peak capacity with some renovations or additional space. An initial license fee of \$3 million for every 500 VLTs is to be submitted by April 15, 2012. Assuming that license applicants opt to participate and pay the license fee for 1,000 VLTs by the required deadline, ETF revenues would increase by \$6 million in fiscal 2012. It is estimated that a VLT facility at BWI will not have a significant negative effect upon VLT revenues at other Maryland VLT facilities due to the location inside the security perimeter and the proportion of out-of-state residents who travel through BWI.

MAA advises that federal law requires the airport to charge rent for terminal space and that a minimum percentage of operator proceeds would have to be paid to the airport. Federal law also places restrictions on the use of revenue generated by the use of airport space that may conflict with the revenue distribution provisions of the VLT program. MAA advises that revenue distribution under the bill could jeopardize \$43 million in annual grant revenue and passenger facility charges related to the federal Airport Improvement Program, as well as an addition \$15 million in federal grant funds.

According to McCarran International's fiscal 2009 financial report, all airport gaming revenue is deposited into the Airport System Capital Fund. Legislative Services' fiscal analysis assumes that there will be an opportunity to distribute the amount of net revenues generated by a BWI facility while complying with federal law.

VLT Revenues

After payouts to winning players, but **before** any other distributions are made, total revenues generated could total approximately \$5.4 million in fiscal 2014 and \$37.1 million in fiscal 2015.

These estimates assume that (1) the facility will initially operate at 50% capacity in April 2014 (two years after bid submission) and reach full capacity one year later; (2) 1,000 VLTs are awarded and can be accommodated at BWI by fiscal 2015. Revenues will be potentially higher (lower) than estimated to the extent that operations begin earlier (later) than estimated in temporary or permanent facilities; and may be higher (lower) than estimated depending on the number of VLTs that BWI can accommodate. To the extent that the Video Lottery Facility Location Commission reallocates any available VLTs to other locations, up to a maximum of 4,750 as authorized in current law, revenues could be higher.

A win per day (WPD) estimate of \$125 at peak capacity for the VLT facility is based on the location, its proximity to likely facilities in Anne Arundel County and Baltimore City, 1,000 VLTs, an average WPD of \$80 at McCarran International in fiscal 2007 through 2009, the relative scarcity of machines in Maryland as compared to Nevada, and the assumption that the average airport passenger is less likely to gamble than the average visitor to a casino. Legislative Services advises that the gross VLT revenue estimate could be higher or lower than estimated depending on the economic and market conditions that develop as the bill is implemented, including expansion of gaming in the surrounding states. Other assumptions used in estimating VLT revenues are:

- VLTs will operate 365 days a year, once operational;
- Virginia and Washington, DC do not authorize VLT gambling; and
- West Virginia and Delaware do not expand their number of VLT facilities.

Exhibit 2 details the revenue distribution resulting from 1,000 VLTs at a BWI facility for fiscal 2011 through 2015.

Exhibit 2
Gross VLT Revenue Projections for BWI

	<u>FY 2012</u>	<u>FY 2013</u>	<u>FY 2014</u>	<u>FY 2015</u>
Education Trust Fund	\$6,000,000*			
Transportation Trust Fund			\$2,627,715	\$17,979,102
Licensee			1,787,930	12,233,203
Local Government			297,988	2,038,867
Small, Minority, & Woman-owned Business			81,270	556,055
Purse Dedication Account			379,258	2,594,922
Racetrack Renewal Account			135,449	926,758
Lottery Operations			108,359	741,406
Total Annual Gross	\$6,000,000	\$0	\$5,417,969	\$37,070,313

*Assumes initial license fee payment for 1,000 additionally authorized VLTs.
Source: Department of Legislative Services

Problem Gambling Fund

Approximately \$425,000 annually beginning in fiscal 2016, based on \$425 per VLT at full implementation of 1,000 VLTs, will be credited to the Problem Gambling Fund administered by DHMH. Approximately \$30,600 will be credited in fiscal 2014 and \$345,300 will be credited in fiscal 2015. The fund must be used to establish a 24-hour hotline, provide counseling for problem gamblers, and establish problem gambling prevention programs and other support services.

Indirect Economic Development Revenues

In addition to the direct revenues generated, the introduction of up to 1,000 VLTs could generate other revenues due to the increased economic activity. As a result of licensure requirements, if 1,000 VLTs are awarded the VLT licensee would undertake at least \$50 million in one-time capital improvements and construction costs.

Any construction jobs associated with VLTs at BWI could bring dollars into the surrounding area, providing an economic boost to the local economy. To the extent that the annual capital improvement activity increases, the local economy will receive a boost from annual capital improvements. New jobs would generate new incomes which would be subject to the income tax – revenues that are not currently generated. If substitute jobs are higher (lower) paying than the previously held jobs, taxes paid by those individuals would be higher (lower) than paid previously.

State Expenditures:

Maryland State Lottery Agency

The Maryland State Lottery Agency will need to procure additional VLTs to be placed in a BWI video lottery facility at an estimated cost of \$511,000 in fiscal 2014 and \$3.3 million in fiscal 2015. Expenditures for the central computer system required for the overall VLT program may increase as well, but the State lottery is unable to estimate the effect at this time. The Maryland State Lottery Agency advises it will need additional employees, including six security investigators, one accountant, and one auditor; Legislative Services estimates that two additional security investigators and one accountant/auditor will be sufficient at a cost of approximately \$200,000 in fiscal 2014, increasing to \$207,000 in fiscal 2015.

From the VLT proceeds generated at BWI, \$108,400 will be distributed to the Lottery Agency in fiscal 2014 and \$741,400 in fiscal 2015 and will be insufficient to pay for increased Lottery expenditures. Accordingly, general fund expenditures will increase by \$429,100 in fiscal 2014 and by \$2.8 million in fiscal 2015.

Effect on Lottery Sales

Legislative Services assumes that 1,000 additional VLTs at BWI would not permanently reduce lottery revenues beyond the 10% reduction already estimated for the authorized VLT program.

Education Trust Fund and Other VLT Fund Expenditures

In light of the substantial structural deficit currently forecasted for fiscal 2011 through 2015, it is assumed that all of the available ETF proceeds received in fiscal 2012 are used to support operating programs and, therefore, offset general fund expenditures.

Special fund expenditures will increase by \$2.7 million in fiscal 2014 and by \$18.4 million in fiscal 2015, which reflects the distribution of VLT proceeds to the licensee of the facility; to local governments; purse dedication and racetrack renewal accounts; and small, minority, and woman-owned businesses.

Infrastructure Costs

The State could incur significant costs associated with infrastructure and transportation upgrades near BWI. The actual impact will depend upon specific plans for any future video lottery facility at BWI. To the extent that only ticketed passengers and BWI employees can access the areas with VLTs, costs would be minimal.

Indirect State Expenditures

In addition to the positive indirect effects to the economy, negative impacts could be expected as well. These effects could include increased levels of crime, unemployment, and personal bankruptcies which could result in a need to significantly increase the State and local spending directed toward these effects. Although these costs cannot be reliably estimated, Legislative Services estimates that these costs are likely to be greater than the funds dedicated to the Compulsive Gambling Fund under this bill. For a more in-depth discussion about the possible social costs as a result of authorizing VLTs, consult the *Legislator's Guide to Video Lottery Terminal Gambling*.

Local Fiscal Effect: Local revenues will increase by \$298,000 in fiscal 2014 increasing to \$2.0 million in fiscal 2015. Of this amount, revenues for local jurisdictions with VLT facilities will increase by approximately \$244,000 in fiscal 2014. Anne Arundel County infrastructure costs may increase due to the BWI facility. The extent of any increased infrastructure expenditures will depend upon specific plans for a video lottery facility and the degree to which needed infrastructure improvements are not covered by State expenditures.

Small Business Effect: To the extent that the VLT facility purchases goods from local businesses that are small businesses, these small businesses will benefit. Small business horse industry breeders and owners in the thoroughbred and standardbred racing industry would benefit. Some small businesses, especially those located in the BWI terminal building, may be harmed as a result of travelers substituting VLT wagering for other expenditures. Expenditures from the Small, Minority, and Woman-owned Business Investment Account will benefit small businesses.

Other small businesses will be harmed by the substantial substitution of consumer spending away from other consumption to gambling. Small businesses in the entertainment and retail food service near VLTs could be particularly harmed.

Additional Comments: Legislative Services notes that the bill may limit the travel options of individuals on either the voluntary or mandatory problem gambling exclusion list, and may somewhat diminish the incentive for individuals to join the voluntary exclusion list.

Additional Information

Prior Introductions: HB 777 of 2009, a similar bill, received a hearing in the House Ways and Means Committee, but no further action was taken.

Cross File: None.

Information Source(s): Comptroller's Office, Maryland State Lottery Agency, Maryland Department of Transportation, Department of Legislative Services

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