

Department of Legislative Services
Maryland General Assembly
2007 Session

FISCAL AND POLICY NOTE

Senate Bill 950 (Senator Miller)
Budget and Taxation

Education Funding Act of 2007

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, 2007.

Fiscal Summary

State Effect: Special fund revenues increase in FY 2008 and beyond due to one-time application fees and VLT revenues. General fund revenues decrease beginning in FY 2009 due to decreased lottery sales; future year losses mount with increased VLT implementation, totaling \$86.6 million in FY 2012. General fund expenditures decrease in FY 2008 and beyond due to the availability of revenues from the ETF. General fund expenditure increase in FY 2008 due to lottery start-up costs and in FY 2009 and beyond due to Attorney General expenses. Special fund revenues and expenditures increase for lottery agency administrative expenses, local aid, purse dedication, bred funds, gambling addiction treatment expenditures, State Police, and education beginning in FY 2009. **Appendix 1** shows the revenues and expenditures by fund in greater detail.

(\$ in millions)	FY 2008	FY 2009	FY 2010	FY 2011	FY 2012
GF Revenue	\$0	(\$1.6)	(\$40.8)	(\$79.9)	(\$86.6)
SF Revenue	93.0	23.0	540.5	1,045.5	1,102.5
GF Expenditure	13.5	66.8	(160.8)	(519.4)	(562.0)
SF Expenditure	0	116.1	540.6	1,045.5	1,102.5
Net Effect	\$79.5	(\$161.5)	\$119.9	\$439.5	\$475.4

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 \$1.7 million in FY 2009, increasing to \$80.6 million at VLT full implementation in FY 2012. 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.

Video Lottery Terminals and Locations

This bill authorizes a total of 15,500 VLTs in the State at seven locations. The VLT facility locations are to be determined by a commission created by the bill. The distribution of VLTs among the facilities is also to be determined by the commission.

The bill reiterates the current prohibition on additional forms of gambling, other than those currently authorized under State law (lottery, horse racing, and charitable gambling). The State Lottery Commission will provide regulation and oversight of the VLT program.

Distribution of Video Lottery Terminals Proceeds

The Comptroller is required to distribute the proceeds of VLT operations, which must be transferred electronically on a daily basis to the State Lottery Fund.

For the four race track locations, from the gross proceeds of VLTs, after pay out to players, proceeds are distributed as follows:

- 5% to the State Lottery Agency for administrative costs (after the first year, the distribution is 4.3%);
- 5% to the local governments in which video lottery facilities are operating;
- 5.1% to the Purse Dedication Account (PDA) to enhance horse racing purses and to provide funds for the horse breeding industry (after the first year, the distribution increases to 5.8%);
- the operators will receive the amount stated on the bid proposals selected by the State Video Lottery Facility Commission, not to exceed 36% to VLT operation licensees; and

- the remainder of the proceeds will be distributed to the ETF established under the bill (a minimum of 48.9%).

For the three nontrack locations, from the gross proceeds of VLTs, after pay out to players, proceeds are distributed as follows:

- 5% to the State Lottery Agency for administrative costs (after the first year, the distribution is 4.3%);
- 5% to the county(s) in which the video lottery facilities operate;
- 5.1% to the Purse Dedication Account (PDA) to enhance horse racing purses and to provide funds for the horse breeding industry (after the first year, the distribution increases to 5.8%);
- the operators will receive the amount stated on the bid proposals selected by the State Video Lottery Facility Commission (not to exceed 30%); and
- the remainder of the proceeds will be distributed to the ETF (a minimum of 54.9%).

Video Lottery Facility Location Commission

This bill creates a Video Lottery Facility Location Commission that will determine the distribution of the 15,500 VLTs among the seven potential licensees and the percentage of operator VLT gross proceeds. Each licensee is eligible for a maximum of 5,000 VLTs, and a maximum of 6,000 VLTs can be awarded to any licenses owned by the same entity. In addition, no more than 7,500 VLTs or two licenses can be located in any county. A race track license and nontrack license may not be awarded to the same individual or entity. An individual or entity cannot be awarded more than two track or nontrack licenses.

Eligible applicants for VLT licenses must submit an application by October 1, 2007. The amount of the initial license fee is equal to \$3 million for each 500 VLTs awarded. License fees accrue to the ETF. The commission is composed of nine members, of whom five are appointed by the Governor, two by the Speaker of the House, and two by the President of the Senate. These nine members elect a chairman. These appointments are subject to the approval of the Legislative Policy Committee.

When considering all facility applications, the commission must consider an application (1) 70% based on business and market factors; (2) 15% economic development factors; and (3) 15% siting factors. No applicant may own or have interest in more than one VLT license. The Department of Budget and Management (DBM) is required to contract with an independent analyst with at least 10 years' experience in gaming industry consulting

that will provide advice on bids to the location commission. Qualified bidders may submit bids according to the competitive sealed process established under Title 13 of the State Finance and Procurement Article.

Lottery Commission Authority and Duties

VLTs will be owned or leased by the State Lottery Commission and under the control of the commission at all times. The membership of the State Lottery Commission increases from five to nine. One member will serve as a liaison to the State Racing Commission and one member of the State Racing Commission will serve as a liaison to the lottery commission.

The commission has authority to issue subpoenas and conduct investigations and hearings and require a bond for faithful performance of the requirements of the bill. Commission employees must be present at VLT facilities during all hours of VLT operation for the purpose of certifying revenue from VLTs and receiving complaints from the public.

VLT Licenses

Licenses must be obtained by VLT operators, VLT manufacturers, VLT employees, and anyone hired by a VLT operator to manage a VLT facility. In addition, the commission may require others to be licensed.

All applicants for VLT-related licenses are subject to an application process that involves a State and national criminal history records check. All applicants for VLT-related licenses must establish their qualifications including financial stability and background of the applicant and all individuals and business entities associated with the applicant; integrity of financial backers and investors; good character and honesty; and sufficient business ability and experience.

A VLT operation license applicant must provide additional information that includes the financial structure of the entity and names, personal history, and criminal history of all officers, partners, and principal employees; the names of all holding companies, subsidiaries, or other business entities of the applicant; and the names of all persons who own or control the business entity as well as a description of all bonus and profit-sharing agreements. It is a misdemeanor offense punishable by up to three years in jail and/or a \$5,000 fine for any person that requires licensure under the bill and knowingly provides false information to the commission.

The term of a VLT operation license is 15 years. At the end of the 15-year term, the licensee may reapply for a license renewal of 10 years, with the fee to be determined by future statute. The bill provides that a VLT-related license is a revocable privilege and that it is the intent of the bill to prohibit the creation of a property right in a license granted under the bill.

Any VLT license issued under the bill may not be transferred, sold, or pledged as collateral. A licensee may not sell or transfer more than 5% of the legal or beneficial ownership in the licensee without the approval of the commission.

VLT licensees must meet the State's minority business participation requirements for facility construction and procurement; and meet the county's minority business participation requirements, to the extent practicable, if they are higher than the State's. VLT licensees must provide health insurance coverage to its employees and have a preference for hiring individuals that live within 10 miles of the VLT facility. From the time of being issued a license, a VLT licensee is required to commence operations within 18 months (the State Lottery Commission is authorized to extend this deadline for up to one year). VLT licensees must propose capital construction expenditures of at least \$15 million for each 500 VLTs.

Additional Requirements for Horse Track VLT Operation Licensees

None of the requirements in this section apply to the nontrack VLT facilities.

As a condition of licensure, a track licensee must maintain the number of live racing days conducted in 2004. If Pimlico or Laurel Park is awarded a license, the VLT operation license of the two tracks would be revoked if either the Preakness Stakes or Woodlawn Vase is transferred out of the State. In addition, the Maryland Million must be conducted annually at Laurel Park. Horse track VLT licensees are authorized to operate temporary VLT facilities but must have VLTs "fully operational" at a permanent facility within two years of being issued a license.

Each track licensee must develop a racing improvement plan to improve the quality and marketing of horse racing at the track.

The plan must include \$1.0 million of annual capital maintenance and improvements of the horse racing facilities for each 1,000 VLTs authorized for the licensee's location. The capital improvements must include the improvements necessary to make residential areas of the tracks conform to minimum county housing and sanitation standards. In addition, part of the capital improvements at Pimlico must include the creation of a premier classic race track and museum.

Other Regulation of Video Lottery Operations and Consumer Protections

The bill prohibits a VLT operation licensee from offering food (except finger food and the like) and beverages, including alcoholic beverages, for free or for a price that is lower than the prices in the county where the VLT facility is located.

The State Lottery Commission must adopt regulations to reduce or mitigate the effects of problem gambling, including provisions that permit self-exclusion from VLT facilities for individuals with gambling problems; limits on the dollar amount that VLT machines will accept; payouts of winnings above a certain amount by check; limits on the number, location, and maximum withdrawal amounts for ATMs; conspicuous disclosures related to VLT payouts and odds; and consumers being given a record of spending levels to the extent that marketing measures that track customer spending are used.

Purse Dedication Account

The bill creates a Purse Dedication Account to which 5.1% of gross VLT proceeds will be distributed in the first year and 5.8% in the following years. Funds from the account are to be distributed between standardbred and thoroughbred racing based on the percentage of total live wagering in the State each type of racing had in the previous year.

From the proceeds allocated to thoroughbred racing:

- 89% to mile thoroughbred purses at Pimlico, Laurel Park, Allegany, and Timonium; and
- 11% to the Maryland-bred Race Fund.

From the proceeds allocated to standardbred racing:

- 89% to standardbred purses at Rosecroft, Ocean Downs, and Allegany; and
- 11% to the Standardbred Race Fund.

Annually \$250,000 is to be dedicated to improving health care for Maryland jockeys. To pay for these benefits, \$125,000 will be deducted annually from both the mile thoroughbred and standardbred purses.

Education Trust Fund

The bill creates an Education Trust Fund (ETF) as a special, nonlapsing fund that will receive an indeterminate share from VLT facilities (at least 48.9% from race tracks and 54.9% from nontrack facilities) to fund the Bridge to Excellence in Public Schools Act of

2002 (Chapter 288 of 2002), including the GCEI, which is mandated and phased in beginning in fiscal 2009. The bill mandates that in fiscal 2009 through 2019, the Governor include at least \$150 million of the ETF received from VLT revenues for K-16 public school construction and capital improvements. In addition, initial application fees will be credited to the fund. The balance of this fund can be used to offset existing education expenditures, provide funds for additional K-16 school contributions, or increase State undergraduate student financial aid.

Local Development Councils and Transportation

From the local development grants provided to the areas where VLT facilities are located, the proceeds are intended to be used for infrastructure improvements, public safety, and other needs in the communities in the immediate proximity of the facility. A Local Development Council would be created in each area where a VLT facility is located to advise, comment, and make recommendations on a plan developed by the county providing for the use of the Local Development Grant funds. Counties must allocate at least 20% of their local development grant to provide grants to minority business enterprise (MBE) small businesses in the county. These grants are to be focused on communities that are economically distressed or in close proximity to a VLT facility.

The bill also provides that the State may pay for the reasonable transportation costs necessary to mitigate the impact on the communities in immediate proximity to the VLT facilities and to make VLT facilities accessible to the public.

Compulsive Gambling Fund

The bill assesses a \$390 fee per VLT terminal to be paid by VLT operation licensees that will be placed into a Compulsive Gambling Fund administered by the Department of Health and Mental Hygiene (DHMH). The fund must be used to establish a 24-hour hotline, provide counseling and other support services for compulsive gamblers, and establish problem gambling prevention programs.

Other Provisions

The bill also requires the Maryland Department of Transportation to review, coordinate, and approve county transportation studies. The Governor's Office of Minority Affairs must monitor compliance with applicable minority participation requirements in VLT procurement and facility construction until June 30, 2010. In addition, two studies must be conducted to evaluate the State's continued compliance with federal and constitutional requirements related to minority participation provisions. The bill prohibits lottery sales at VLT facilities.

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*.

Background: Over the past several legislative sessions, various proposals have been introduced to authorize VLTs at the State's horse racing tracks or other tourist destinations in the State. Numerous states have authorized VLT gambling. For more information on prior year introductions and other state VLT regimes, consult the *Legislators' Guide to Video Lottery Terminal Gaming*.

One of the recommendations of the Commission on Education Finance, Equity, and Excellence (Thornton Commission) was to adjust State aid to reflect regional differences in the cost of education that are outside the control of local jurisdictions. The Thornton Commission defined adequate funding as revenues sufficient to acquire the resources needed to reasonably expect that students can meet the State's academic performance standards. Because these resources cost different amounts in different places, the Thornton Commission recommended that State aid be adjusted to account for the variations. However, the commission did not believe that an acceptable index existed at the time it was completing its work. The commission recommended that the Maryland State Department of Education (MSDE) contract with a private entity to develop a Maryland-specific index to be used to adjust State aid beginning in fiscal 2005. This recommendation was codified in the Bridge to Excellence in Public Schools Act of 2002.

The consultants hired by MSDE submitted a final report entitled *Adjusting for Geographic Differences in the Cost of Educational Provision in Maryland* on December 31, 2003. The report includes a GCEI with index values that range from 0.948 in Garrett County to 1.048 in Prince George's County. The Budget Reconciliation and Financing Act (BRFA) of 2004 (Chapter 440) codified the index recommended by the consultants except that no adjustment in aid is made for counties that have an index value below one. The 2004 BRFA did not mandate funding for the index and provided that if the index was not fully funded the amount distributed to each jurisdiction would be proportional to what would have been funded at the full level. The Governor's fiscal 2008 allowance includes no funding for the GCEI. SB 950 mandates phased-in funding of the GCEI beginning in fiscal 2009.

The bill also requires the Governor to include at least \$150 million in the annual budget from the ETF for public school construction and higher education capital improvements

in fiscal 2009 through 2016. The Public School Facilities Act of 2004, Chapters 306 and 307 of 2004, set a goal to fully fund school construction by fiscal 2013 to meet minimum required standards for new construction as of July 2003. Based on the work of the Task Force to Study Public School Facilities the total cost to meet standards is estimated at \$3.85 billion with the State's share at approximately \$2 billion and local governments' share at \$1.85 billion.

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, 2007. 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 2008.

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.

These estimates assume that (1) four licenses will be awarded to race tracks and three licenses will be awarded to nontrack facilities; (2) each VLT facility will average \$285 win-per-day; (3) facilities will initially operate at 50% capacity and reach full capacity one year later; and (4) all 15,500 VLTs are awarded. It is assumed that the nontrack locations begin operations January 2010 and horse track locations begin operations in June 2009. Revenues will be potentially higher than estimated in fiscal 2008 and 2009 to the extent that (1) facilities begin operations earlier than estimated; and/or (2) race track operators receive approval to operate temporary facilities.

The Department of Legislative Services (DLS) advises that the final location of the facilities may substantially alter both the total revenue and distribution thereof generated by the seven VLT facilities. These estimates have taken into consideration some degree of competition between the central Maryland facilities. To the extent that a VLT facility is located in close proximity to another VLT facility, total gross proceeds could be substantially less.

Win-per-day estimates are based on previous estimates of the market for VLTs in Maryland and are adjusted by DLS to reflect the effects of the additional machines at nontrack facilities and authorization of VLT facilities in Pennsylvania. For a comparison of these revenue estimates and the market for VLTs in Maryland with several other VLT markets, see **Appendix 2**. The win-per-day estimates for the facilities are the average of the three central Maryland track facilities. To the extent that win-per-days are higher at the nontrack facilities, relative to the race track facilities, annual revenues to the ETF will be greater.

It is assumed that race track VLT operators will receive 36% of gross proceeds and nontrack VLT operators will receive 30% of gross proceeds. As a result, it is assumed that at least 48.9% of the gross proceeds from the race track facilities will go to the ETF (54.9% for nontrack locations). To the extent that market forces cause facilities to accept less than the respective maximum shares, then the ETF revenues could be higher. Operations reach full capacity at all facilities in fiscal 2012, at which point it is assumed the ETF receives 52.9% of annual gross revenues.

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 1 details the revenue distribution resulting from VLTs for fiscal 2009 through 2012.

Exhibit 1
Distribution of Annual VLT Revenues
(\$ in Millions)

	<u>FY 2009</u>	<u>FY 2010</u>	<u>FY 2011</u>	<u>FY 2012</u>
Total Gross	\$33.6	\$814.6	\$1,536.8	\$1,612.4
ETF	16.4	412.6	807.4	853.0
Licensees	12.1	279.0	497.3	516.0
PDA	1.7	42.0	86.8	93.5
Local	1.7	40.7	76.8	80.6
Lottery Operations	1.7	40.3	68.4	69.3

Effect on Lottery Sales

DLS estimates that VLTs, when fully implemented, will cause a permanent reduction in lottery revenues of 15% 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 2** 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 2
Estimated Loss in General Fund Revenue
Due to Decreased State Lottery Sales
(\$ in Millions)

<u>FY 2009</u>	<u>FY 2010</u>	<u>FY 2011</u>	<u>FY 2012</u>
\$1.6	\$40.8	\$79.9	\$86.6

The Lottery Agency estimates that lottery revenues would decline by 1% in fiscal 2008, 5% in fiscal 2009, 3% in fiscal 2010, and 1% in fiscal 2011 before rebounding in fiscal 2012 and beyond.

Compulsive Gambling Fund

Approximately \$6.0 million annually, based on \$390 per VLT at full implementation, will be credited to the Compulsive Gambling Fund administered by DHMH. The fund must be used to establish a 24-hour hotline, provide counseling and other support services for compulsive gamblers, and establish problem gambling prevention programs.

DHMH advises that beginning in the year when all VLTs are awarded, the money credited to the Compulsive Gambling Fund will be distributed as follows:

Statewide Hotlines	\$200,000
Gambling Prevention Effort	500,000
Outpatient Treatment Services	3,741,500
Residential Treatment Services	<u>1,603,500</u>
Total	\$6,045,000

Indirect State Revenues

Economic Development Impacts

In addition to the direct revenues generated, the introduction of VLTs could generate other revenues due to the increased economic activity associated with VLTs. As a result of the licensure requirements in this bill, if the maximum 15,500 VLTs are awarded VLT facilities would undertake \$465 million in one-time capital improvements and construction costs. In addition, if all four horse track licenses are awarded, race track facilities would spend \$4.0 million annually for capital improvements to the horse racing track facilities.

The construction jobs associated with track improvements could bring dollars into the areas surrounding the tracks, providing an economic boost to the local economy. Construction costs of \$481 million compare roughly to the cost of building two professional football stadia. To the extent that the annual capital improvements are not being currently done, 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.

Substitution and Cross-border Effects

The group of potential VLT players at a Maryland facility can be divided into four cohorts. The theoretical impact of each of these cohorts on direct and indirect revenues to the State are illustrated in **Exhibit 3**.

Exhibit 3 **Cross-border and Substitution Effect Impacts**

<u>Cohort</u>	<u>Cross-border and/or Substitution Impact</u>
Marylanders who currently travel out-of-state to play VLTs	Additional direct and indirect revenue to the State
Marylanders who do not currently travel out-of-state to play VLTs but would play in Maryland	Additional direct revenue to the State, offset by any lost revenue from substitution effects
Out-of-state residents who currently play VLTs elsewhere but who would come to Maryland to play VLTs	Additional direct and indirect revenues to the State
Out-of-state residents who do not currently play VLTs elsewhere but who would come to Maryland to play VLTs	Additional direct revenue to the State. If VLT spending substitutes for other consumption in Maryland, then other tax revenues could decline

For all four cohorts, direct revenue to the State increases as a result of VLT gambling. Indirect State revenues increase as a result of (1) the recapture of Marylanders who play VLTs out-of-state; and (2) out-of-state residents who travel to Maryland explicitly to play VLTs and would not have otherwise visited Maryland in the absence of VLTs.

Indirect State revenues decrease as a result of out-of-state residents and Marylanders who substitute playing VLTs for other forms of taxable activities. For instance, out-of-town conventioners may opt to go to Pimlico and play VLTs instead of attending an Orioles game. In this case, the State gains VLT gaming revenue but would lose the admissions and amusement tax that would have been generated if the conventioner attended the Orioles game. Part of the substitution effect for Marylanders is captured by the estimated decline in lottery revenues resulting from individuals opting to play VLTs instead of purchasing lottery tickets. To the extent that Marylanders substitute playing VLTs for additional forms of taxable entertainment and consumption, indirect State revenues will decrease further. Examples of this include a Marylander opting to play VLTs instead of going to a bar or out to dinner which generate alcohol and sales taxes respectively.

Estimates vary as to the share of total VLT revenues that each cohort will contribute. Of particular interest has been the amount of VLT revenue that would be recaptured from Marylanders playing VLTs in neighboring states. Legislative Services estimates that approximately \$390 million or approximately one-quarter of total revenue generated by West Virginia and Delaware VLT facilities comes from Marylanders. Further, it is estimated that these Marylanders contribute approximately \$150 million in revenue to West Virginia and Delaware local and state governments. Authorizing VLTs will not recapture all of this revenue; the amount of players that would be recaptured depends on multiple factors, including the ultimate location of the nontrack facilities. In addition, Pennsylvania has opened 4 VLT facilities since November 2006 and has approved 11 additional VLT facilities, which could impact the annual revenue “recaptured” by Maryland VLT facilities.

State Expenditures:

Administrative Expenditures

Lottery Agency

The Lottery Agency states that it will need 46 additional employees. The agency estimates a budget request of approximately \$13 million will be needed for fiscal 2008 to pay for start-up costs associated with VLT operations. Administrative costs for the State lottery to operate video terminals would be approximately \$1.7 million in fiscal 2009. This estimate assumes that the cost of leasing and maintaining VLT terminals and central computer system as well as providing for additional staff will be equal to approximately 5% of gross revenues in the first year and 4.3% of gross revenues in the following years. Lottery Agency administration expenses are assumed to be consistent with the percent of gross proceeds allocated to it, so no net effect is assumed. To the extent that expenses are higher or lower than estimated, the net effect could change accordingly. If administration expenses are less than the amount allocated in each year under the bill, the additional gross proceeds from VLT facilities would be split equally between the PDA and the ETF.

Attorney General

The Office of the Attorney General would incur increased general fund expenditures of approximately \$259,600 in fiscal 2009 as a result of hiring two assistant Attorneys General and one legal secretary to provide legal support to the VLT program.

Department of State Police

The Department of State Police would incur increased general fund expenditures of approximately \$639,400 in fiscal 2009 as a result of equipment costs and hiring four

full-time troopers, one corporal, and one office secretary to handle the anticipated volume of background checks.

Maryland Department of Transportation

The bill requires the Maryland Department of Transportation (MDOT) to study the impact of increased traffic resulting from VLTs at Pimlico Race Course and submit the findings of the report to the General Assembly by December 1, 2007. Pimlico Race Course is required to pay for this study. The bill also requires MDOT as the State’s MBE certifying agency, to conduct a study regarding specified aspects of the minority business enterprise requirements of the bill and report to the Legislative Policy Committee by December 1, 2010 for the first study and by September 30, 2012 for the second study. MDOT did not provide an estimated cost of the studies. Legislative Services estimates that the studies will cost \$50,000 each.

Education Expenditures

As shown in **Exhibit 4**, most State VLT revenues and initial license fees are dedicated to the ETF to be used for public education programs associated with the Bridge to Excellence in Public Schools Act of 2002 (Chapter 288). This bill increases education aid beginning in fiscal 2009 by (1) requiring the Governor to include \$150 million annually from the ETF in fiscal 2009 through 2019 for public school construction and higher education capital projects; and (2) phasing in the GCEI statutory formula over three years, reaching full funding in fiscal 2011. Under current law, the GCEI is funded to the extent provided in the State budget.

It is assumed that, after satisfying the \$150 million mandate for capital, the remaining ETF revenues from VLT operations will be available to fund education aid including the mandated GCEI. This will result in an equivalent decrease in general fund expenditures.

Exhibit 4
Education Funding Provided by SB 950
Fiscal 2008 through 2012

	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY 2010</u>	<u>FY 2011</u>	<u>FY 2012</u>
Total ETF Funds	\$93.0	\$16.4	\$412.6	\$807.4	\$853.0
School Construction	0	109.4	150.0	150.0	150.0
GCEI Funding Provided by SB 950	0	65.9	101.1	137.2	140.1
Impact on GF Expenditures	\$0	\$65.9	(\$161.5)	(\$520.2)	(\$562.9)

Fiscal 2009 ETF revenues are estimated to not be sufficient to fund the mandated amount for the GCEI and school construction. It is assumed that although the bill mandates that the Governor include \$150 million in the budget for school construction, funding will be provided only to the extent of total revenues in the ETF. Initial VLT license fees accrue to the ETF in fiscal 2008. It is assumed that these funds are expended for public school construction in fiscal 2009. **Appendix 3** lists a breakdown of GCEI funding by jurisdiction provided by the bill in fiscal 2009 and beyond.

Infrastructure Costs

The State and local governments could also incur significant costs associated with infrastructure upgrades at each of the race tracks and nontrack locations. The actual costs are site specific and could range from adding more traffic signs and lights to significantly altering existing traffic routes and adding access from other major thoroughfares. MDOT states that estimating these costs is not possible until plans are developed and traffic studies are completed.

DHMH Expenditures – Prevalence Study

DHMH estimates that a prevalence study will cost up to approximately \$1.2 million. This estimate is based on conducting a four-month study that samples 38,000 Marylanders or approximately 1% of the State adult population. DLS estimates that the first study required would cost approximately \$500,000 to conduct.

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, DLS 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 Revenues: The bill provides local impact aid for jurisdictions in which VLT operations are located. This aid is to be used for infrastructure, facilities, services, and other improvements and grants to MBE businesses. For all facilities except Laurel Park, 5% of gross proceeds will be distributed to the county in which they are located. Of the 5% of VLT gross proceeds generated by Laurel (if it receives a license), Anne Arundel County is to receive 73%, Howard County 17%, and Laurel 10%. Based on the assumed VLT-implementation schedule, local aid will total \$1.7 million in fiscal 2009,

\$40.7 million in fiscal 2010, \$76.8 million in fiscal 2011, and \$80.6 million in fiscal 2012. **Exhibit 5** shows the local aid that would be distributed at full implementation for different sized VLT facilities.

Exhibit 5
Local Revenue Distributions at Full Implementation

<u>Number of VLTs</u>	<u>5% Local Distribution</u>
1,000	\$5.2
1,500	7.8
2,000	10.4
2,500	13.0
3,000	15.6
3,500	18.2
4,000	20.8
4,500	23.4
5,000	26.0

Indirect Local Revenues

The local jurisdictions where VLT facilities are located would also benefit from increased real property tax collections. In addition, if the Lottery Agency decides to lease VLTs from a VLT manufacturer, local jurisdictions would benefit from increased personal property taxes assessed on VLT machines and paid by the lessor. To the extent that expenditures on items subject to admissions and amusement taxes are transferred to VLT wagering, local revenues could decline. Local revenues would also be affected by any changes in property values, positive or negative, occurring because of the introduction of VLTs. This effect cannot be reliably estimated at this time.

Local Expenditures: VLT facilities will have a substantial impact on the local areas in which they are located and will necessitate additional local expenditures. For example, Dover Downs and Delaware Park each attracted over 2 million visitors in 2003. These facilities have approximately 2,000 VLTs, substantially less than the maximum of 5,000 VLTs proposed at four Maryland horse tracks.

Local governments must provide matching funds in order to receive State school construction funds. The local match currently ranges from 3% to 50% of eligible school construction costs, depending on the county.

Baltimore City estimates that if Pimlico is granted a license the annual operating costs for public safety, sanitation, and transportation would total approximately \$9.7 million. In addition to these recurring costs, the city estimates approximately \$1.9 million in one-time operating start-up costs to acquire equipment. It is also estimated that approximately \$65 million in transportation-related capital improvements would be necessary to accommodate the expected influx of activity in and around Pimlico Raceway. These improvements include intersection improvements, signal system installations, and street widening and rehabilitation.

Prince George's County advises that if Laurel and Rosecroft are awarded licenses it would incur expenditures of up to \$20 million in one-time costs and \$4.2 million annually as a result of infrastructure improvements and expanded public services.

The City of Laurel estimates that expenditures would increase by approximately \$1.2 million annually if Laurel Park is awarded a license. This reflects hiring additional police and public works personnel as well as other operating costs. Howard County states that if Laurel Park is awarded a license, the county would need to hire additional police personnel and widen access roads to Laurel Park.

Anne Arundel County estimates that the annual operating costs for public safety, infrastructure, and social services would total \$9 million if Laurel Park is awarded a license. In addition to these recurring costs, the county estimates approximately \$1 million in one-time operating start-up costs to acquire equipment

In addition, the nontrack VLT facilities will likely impose substantial local expenditures in the county(s) in which they are located.

Small Business Effect: DLS advises that to the extent that VLT facilities purchase goods from local businesses that are small businesses, these small businesses would benefit. Small business horse industry breeders and owners in the thoroughbred and standardbred racing industry would benefit. Some small businesses would benefit from additional tourists, partially offset by some small businesses that would be harmed as a result of tourists substituting VLT wagering for other expenditures.

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 VLT facilities could be particularly harmed.

Additional Information

Prior Introductions: SB 225 of 2006, a similar bill, was scheduled for a hearing in the Senate Budget and Taxation Committee, but the hearing was cancelled. Similar bills were introduced in 2005 as SB 205/HB 255. SB 205 received a favorable with amendments report from Budget and Taxation and passed the Senate but was not reported from the House Ways and Means Committee. HB 255 received an unfavorable report from Ways and Means. HB 1361 of 2005 was passed by the House and amended in the Senate to be identical to SB 205, but the differences in the House and Senate versions were not reconciled.

Cross File: None.

Information Source(s): Allegany County, Anne Arundel County, Baltimore City, Prince George's County, Howard County, City of Laurel, Maryland State Lottery Agency, Maryland State Department of Education, Department of State Police, Department of Health and Mental Hygiene, Office of the Attorney General, Maryland Department of Transportation, Innovation Group, State Department of Assessments and Taxation, Department of Legislative Services

Fiscal Note History: First Reader - March 5, 2007
ncs/rhh

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Appendix 1

	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>
Gross VLT Revenues	\$0	\$33,591,406	\$814,591,602	\$1,536,806,836	\$1,612,387,500
Licensees	\$0	\$12,092,906	\$278,976,629	\$497,320,770	\$515,964,000
Special Fund Revenues					
Education Trust Fund	\$0	\$16,426,198	\$412,611,641	\$807,428,234	\$852,952,988
Purse Dedication Account	0	1,713,162	42,014,451	86,842,183	93,518,475
Compulsive Gambling	0	1,511,250	4,911,563	6,045,000	6,045,000
Local Distributions	0	1,679,570	40,729,580	76,840,342	80,619,375
Lottery VLT Administrative	0	1,679,570	40,259,300	68,375,307	69,332,663
License Fees - to ETF	93,000,000				
Total SF Revenues	\$93,000,000	\$23,009,750	\$540,526,535	\$1,045,531,066	\$1,102,468,501
GF Revenues					
Lost Lottery Revenue	0	(1,623,478)	(40,845,260)	(79,947,267)	(86,604,150)
Total GF Revenues	\$0	(\$1,623,478)	(\$40,845,260)	(\$79,947,267)	(\$86,604,150)
Special Fund Expenditures					
Education Trust Fund	0	\$109,426,198	\$412,611,641	\$807,428,234	\$852,952,988
Purse Dedication Account	0	1,713,162	42,014,451	86,842,183	93,518,475
Compulsive Gambling	0	1,511,250	4,911,563	6,045,000	6,045,000
Local Distributions	0	1,679,570	40,729,580	76,840,342	80,619,375
Lottery VLT Administrative	0	1,679,570	40,259,300	68,375,307	69,332,663
Transportation - Studies	0	50,000	50,000		
Total SF Expenditure	0	116,059,750	540,576,535	1,045,531,066	1,102,468,500
GF Expenditures					
Attorney General	0	259,611	273,972	289,282	305,619
State Police	0	639,427	462,783	472,451	599,293
GCEI	0	65,934,044	101,054,931	137,226,910	140,055,935
DHMH - Prevalence Study	500,000				
Education - from ETF	0	0	(\$262,611,641)	(\$657,428,234)	(\$702,952,988)
Lottery VLT Administrative	13,000,000				
Total GF Expenditures	\$13,500,000	\$66,833,082	(\$160,819,955)	(\$519,439,591)	(\$561,992,141)
Net Effect	\$79,500,000	(\$161,906,560)	\$119,924,695	\$439,491,665	\$475,387,991

*In fiscal 2009, ETF revenues are not sufficient to fully fund the mandated appropriations for school construction and the GCEI. It is assumed that funds are expended for public school construction only to the extent provided by the ETF.

Appendix 2
Maryland VLT Market Comparisons

	<u>St. Louis</u>	<u>Chicago</u>	<u>Kansas City</u>	<u>Maryland</u>
VLTs	9,204	\$13,455	6,200	15,500
VLT Revenue (millions)	\$772.7	\$1,941.43	\$455.5	\$1,612.39
Table Revenue (millions)	\$105.7	\$377.9	\$70.2	N/A
Estimated Direct State and Local Revenues	\$270.0	\$888.7	\$145.2	\$939.6
Estimated Tax Rate	31%	38%	28%	58%
Win-per-day	\$230	395	\$201	\$285
Total Population (millions)	2.6	8.3	1.8	5.5
Population over Age 21 (millions)	1.8	5.8	1.3	3.9
Population over 21 per VLT	199	431	206	250
VLT Revenues per Person over 21 Years Old	\$422	\$335	357	416
Percent over Age 65	12%	10%	11%	11%
Median Age	37.1	34.4	35.6	36.9
Percent White	78%	68%	81%	62%
Percent Black	19%	18%	13%	28%
Percent Hispanic	2%	19%	6%	5%
Median Household Income	\$46,803	\$53,462	\$47,428	\$57,218
Percent Below Poverty	10.0%	10.6%	9.1%	8.2%
Unemployment Rate	7.0%	8.8%	7.4%	4.5%
Percent with College Education or Higher	28%	32%	31%	31%

Revenues are estimated for Maryland and are for fiscal 2012, other data are from 2005 or fiscal 2004.

Source: Missouri, Illinois, Indiana Gaming Commissions; U.S. Census Bureau

**Appendix 3
GCEI Expenditures
Mandated by SB 950
Fiscal 2008-2012**

<u>County</u>	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY 2010</u>	<u>FY 2011</u>	<u>FY 2012</u>
Allegany	\$0	\$0	\$0	\$0	\$0
Anne Arundel	0	4,446,365	6,811,158	9,300,256	9,511,139
Baltimore City	0	11,396,945	17,109,684	22,743,263	22,756,984
Baltimore	0	2,795,877	4,274,481	5,798,320	5,924,574
Calvert	0	1,241,113	1,917,025	2,622,636	2,700,214
Caroline	0	0	0	0	0
Carroll	0	1,371,425	2,109,405	2,878,459	2,956,309
Cecil	0	0	0	0	0
Charles	0	1,808,462	2,809,116	3,855,142	3,984,314
Dorchester	0	0	0	0	0
Frederick	0	3,316,726	5,147,474	7,107,496	7,357,736
Garrett	0	0	0	0	0
Harford	0	0	0	0	0
Howard	0	2,519,868	3,897,833	5,336,769	5,461,193
Kent	0	74,184	109,872	146,249	146,652
Montgomery	0	15,888,023	24,531,960	33,644,787	34,649,774
Prince George's	0	20,677,966	31,720,250	42,946,028	43,729,358
Queen Anne's	0	286,277	444,718	610,607	632,039
St. Mary's	0	110,813	171,955	236,898	245,649
Somerset	0	0	0	0	0
Talbot	0	0	0	0	0
Washington	0	0	0	0	0
Wicomico	0	0	0	0	0
Worcester	0	0	0	0	0
Total	\$0	\$65,934,044	\$101,054,931	\$137,226,910	\$140,055,935