

Department of Legislative Services
2011 Session

FISCAL AND POLICY NOTE

Senate Bill 4

(Senators Klausmeier and Glassman)

Budget and Taxation

**Gaming - Slot Machines - Ownership and Operation by Eligible War Veterans'
Organizations**

This bill authorizes all counties to license slot machines that are owned and operated by bona fide war veterans' organizations that have been located in the State for at least five years. Other provisions of current law regarding licensing of up to five slot machines per organization and administrative procedures continue to apply. The eligible nonprofit organizations currently authorized to operate slot machines in eight Eastern Shore counties remain in law.

Fiscal Summary

State Effect: Potential decrease in special fund revenues and expenditures from the Video Lottery Terminal (VLT) program beginning in FY 2012. Under one set of assumptions, State revenues may decrease by \$2.1 million annually, with approximately one-half needing to be replaced with general funds to support mandated expenses. General fund revenues from lottery sales may decrease in the counties that license new slot machines under the bill. Under one set of assumptions, general fund revenue may decrease by approximately \$750,000 annually beginning in FY 2012. The Comptroller's Office can collect additional reports with existing resources.

Local Effect: Potential minimal revenue increase to the extent that the 16 counties not currently authorized to license slot machines elect to do so. Counties will collect \$50 in licensing fees from eligible war veterans' organizations for each slot machine license. Counties that earn revenues from paper gaming but do not currently license slot machines may experience decreased revenue from paper gaming due to competition from slot machines. Potential increase in expenditures for counties that elect to license slot machines. VLT program local impact grant funds may be reduced minimally for those counties with operating VLT facilities.

Small Business Effect: Minimal.

Analysis

Current Law: Generally, it is a misdemeanor crime to possess or operate a slot machine in Maryland. However, legislation was enacted in 1987 and 2007 authorizing certain nonprofit organizations to operate slot machines in the following eight Eastern Shore counties: Caroline, Cecil, Dorchester, Kent, Queen Anne's, Somerset, Talbot, and Wicomico. The 1987 legislation required a nonprofit organization to be located in the county for at least five years prior to the application for a license and to be a fraternal, religious, or war veterans' organization.

Chapter 645 of 2007 expanded the list of eligible organizations that may be licensed to operate slot machines to include those that have been affiliated with a national fraternal organization for less than 5 years but have been located within an eligible county for at least 50 years before applying for a license.

In order to operate a slot machine, an organization must obtain a license from the sheriff's office and pay a fee of \$50 per machine annually to the applicable county. An organization may not own more than five slot machines and must own each slot machine in operation. The slot machines must be located at the principal meeting hall of the organization and cannot be operated at a private commercial facility. The slot machine must be equipped with a tamperproof meter or counter that accurately records gross receipts.

At least one-half of the proceeds generated from slot machines must go to charity. The remainder of the proceeds must go to the organization. An individual cannot benefit financially from the proceeds. The organization must keep accurate records of gross receipts and payouts from slot machines and must report annually under affidavit to the Comptroller's Office the disposition of these proceeds. The Comptroller's Office, however, does not have authority to audit these reports.

VLT Program

During the 2007 special session, the General Assembly adopted two pieces of legislation pertaining to VLT gambling – Chapter 4 (Senate Bill 3) and Chapter 5 (House Bill 4). Chapter 5 was a constitutional amendment approved by the voters at the November 2008 general election that authorized the expansion of gambling subject to specified restrictions. The constitutional amendment provided that (1) a maximum of five VLT facility licenses may be awarded within specified areas of the State; (2) no more than one facility license may be awarded in any county or Baltimore City; (3) a maximum of

15,000 VLTs may be authorized; and (4) VLT facilities must comply with any applicable planning and zoning laws of a local jurisdiction. Chapter 4, which was contingent on ratification of Chapter 5, established the operational and regulatory framework for the VLT program. Chapter 624 of 2010 made several changes to the VLT program implemented by Chapter 4.

Under Chapter 4, VLT facility operation licenses are awarded by the Video Lottery Facility Location Commission. The State Lottery Commission oversees VLT operations and owns/leases VLTs and a central monitor and control system. Chapter 4 allows for a maximum of 15,000 VLTs, distributed as follows: 4,750 VLTs in Anne Arundel County; 3,750 VLTs in Baltimore City; 2,500 VLTs in Worcester County; 2,500 VLTs in Cecil County; and 1,500 VLTs in Allegany County (Rocky Gap State Park).

Background: In fiscal 2008, 52 nonprofit organizations on the Eastern Shore operated slot machines. These organizations donated approximately \$3.6 million to charity. About 67% of these organizations are war veterans' organizations (*e.g.*, American Legion and Veterans of Foreign Wars). Unaudited reports with complete data were available for 50 of the organizations. The total amount bet at these 50 organizations was approximately \$52 million, 87% of which was returned to gamblers. Of the approximately \$6.6 million in net proceeds, \$3.3 million (51%) was disbursed to charity. The Department of Legislative Services (DLS) notes that in reviewing the fiscal 2008 data, it appeared that several organizations were not in compliance with the 50% charity requirement or misclassified some contributions as charitable. Several organizations submitted returns that were incomplete or mathematically incorrect.

The Maryland State Lottery Agency conducted a study of local gaming in Maryland required by Chapter 474 of 2008. The report indicates (similar to DLS findings) that in fiscal 2008, 273 slot machines on the Eastern Shore generated \$54.8 million in total "handle" or bets. **Exhibit 1** shows the slot machine handle by county. The report also showed some relationship between State lottery sales and the existence of local gaming activities. However, the specific relationship between lottery sales and local slot machines was difficult to determine and very weak. **Exhibit 2** shows lottery sales by jurisdiction in fiscal 2010. Overall, 95% of lottery sales in fiscal 2010 were made in the 16 counties that could be affected by this bill.

Exhibit 1
Slot Machine Handle for Eastern Shore Counties
Fiscal 2008
(\$ in Millions)

<u>County</u>	<u>Slot Machines</u>	<u>Handle*</u>
Caroline	20	\$2.4
Cecil	55	14.9
Dorchester	30	4.5
Kent	25	1.5
Queen Anne's	30	6.3
Somerset	24	2.5
Talbot	30	4.6
Wicomico	59	18.0
Total	273	\$54.8

*Numbers may not sum to the total due to rounding.

Source: Maryland State Lottery Agency

Paper gaming, including punch boards, instant bingo, and tip jars, provides two sources of revenues to counties: the sale of paper gaming licenses and tickets to operators; and taxes on paper gaming sales. The Maryland State Lottery Agency advises that paper gaming occurs in at least 15 Maryland counties, and is most prevalent in Allegany, Frederick, Garrett, and Washington counties.

VLT Program Implementation

The Video Lottery Facility Location Commission has awarded video lottery operation licenses for VLT facility locations in Anne Arundel, Cecil, and Worcester counties. Penn Cecil in Cecil County opened in late September 2010 with 1,500 VLTs and Ocean Downs in Worcester County opened in January 2010 with 750 (increasing to 800 in the near future) VLTs. Power Plant Entertainment (PPE) Casino Resorts, LLC was awarded a license in December 2009 to operate a 4,750 VLT facility adjacent to Arundel Mills Mall in Anne Arundel County, contingent upon local zoning approval. County officials subsequently approved zoning legislation, but the legislation was petitioned to a local voter referendum at the November 2010 election. Anne Arundel County voters approved the legislation, allowing the VLT facility to go forward. PPE plans to open a 2,000 VLT temporary facility by the end of 2011 with a permanent facility scheduled to open by the end of 2012. The licenses for Baltimore City and Rocky Gap State Park are yet to be awarded.

State Fiscal Effect: State special fund revenues and expenditures may be reduced, depending on the degree to which eligible war veterans' organizations are licensed to operate slot machines. These machines may serve as a substitute for gambling at VLT facilities in the State, particularly in counties where VLT facilities will be located.

Gambling at the newly eligible nonprofit organizations will represent a shift of spending from other activities, a portion of which are taxable by the State. Numerous studies have examined the relationship between expanded VLT gambling and the substitution effect this expansion has on existing VLT revenues or other State revenues such as the lottery and sales tax. Most of these studies conclude that although total revenues might increase from expanded gambling there is a negative impact on existing revenue streams that partially offsets the revenue from expanded gambling. For example, DLS estimates that VLTs, when fully implemented, will cause a permanent 10% reduction in annual revenues from lottery sales.

The average annual revenue generated from existing gambling at eligible nonprofits is approximately \$130,000 (*i.e.*, total handle minus total amount returned to players) per organization. The bill will add an estimated 160 organizations (an average of 10 per newly authorized county) offering slots play; assuming 5 machines at each results in 800 slot machines generating approximately \$21 million in revenue annually. A small portion of this would likely have otherwise been spent at State VLT facilities. If that portion is 10%, the result is an annual loss of \$2.1 million in special fund revenues. The impact to the State includes a \$1 million reduction in Education Trust Fund revenues and a \$42,000 loss in revenues for State lottery administration of the VLT program. These lost revenues will likely need to be replaced with general funds to cover mandated K-12 education aid and VLT lease costs. **Exhibit 3** shows the reduction in special fund distributions from the total reduction of \$2.1 million illustrated above and based on the distribution of VLT revenues from facilities other than Rocky Gap.

Exhibit 2
State Lottery Sales by County
Fiscal 2010

<u>County</u>	<u>Total Sales</u>	<u>% Of Sales</u>
Allegany	\$10,715,258	0.63%
Anne Arundel	173,999,349	10.20%
Baltimore	278,857,734	16.34%
Calvert	23,437,707	1.37%
Caroline	7,136,091	0.42%
Carroll	34,262,344	2.01%
Cecil	21,368,526	1.25%
Charles	54,698,152	3.21%
Dorchester	8,578,248	0.50%
Frederick	36,068,383	2.11%
Garrett	3,297,026	0.19%
Harford	60,368,798	3.54%
Howard	46,782,605	2.74%
Kent	4,219,742	0.25%
Montgomery	166,297,020	9.74%
Prince George's	342,970,457	20.10%
Queen Anne's	11,323,166	0.66%
St. Mary's	35,773,325	2.10%
Somerset	6,390,263	0.37%
Talbot	8,463,852	0.50%
Washington	25,831,088	1.51%
Wicomico	20,378,999	1.19%
Worcester	24,759,976	1.45%
Baltimore City	300,594,473	17.61%
Total	\$1,706,572,575	100.00%

Numbers do not sum to the total due to rounding.

Source: Maryland State Lottery Agency

Exhibit 3
Illustration of Reduced VLT Program Distribution

Education Trust Fund (48.5%)	\$1,018,500
Licensees (33%)	693,000
Purse Dedication Account (7%)	147,000
Local Impact Grants (5.5%)	115,500
Racetrack Renewal (2.5%)	52,500
Lottery Operations (2%)	42,000
Minority Business Investment (1.5%)	31,500
Total Reduction	\$2,100,000

The impact of new slot machines on lottery sales and revenue is difficult to quantify. The magnitude of the impact will depend on the number of counties that choose to license slot machines and the location of the machines, as well as the substitution of slot machine for lottery spending. As noted, Legislative Services has estimated a permanent 10% reduction in lottery sales with full VLT program implementation (approximately \$1.4 billion in total revenues). Applying this assumption to the scenario described above (\$21 million in revenue from 800 slot machines), lottery sales will decrease by 0.15%, which equates to a general fund revenue reduction of approximately \$750,000 annually.

Additional Information

Prior Introductions: SB 4 of 2010 received a hearing in the Senate Budget and Taxation Committee, but no further action was taken. Its cross file, HB 663, received an unfavorable report from the House Ways and Means Committee. Several similar bills have been introduced since the 2006 session. SB 49 and SB 102 had a hearing in the Senate Budget and Taxation Committee in the 2009 session, but no further action was taken. HB 608 of 2009 received a hearing in the House Ways and Means Committee, but no further action was taken. SB 29 of 2008 received an unfavorable report from the Senate Budget and Taxation Committee. SB 98 of 2007 had a hearing in the Senate Budget and Taxation Committee, but no further action was taken. SB 132 of 2006 was scheduled for a hearing by the Senate Budget and Taxation Committee, but the hearing was cancelled. Its cross file, HB 884, received an unfavorable report from the House Ways and Means Committee.

Cross File: HB 735 (Delegate Weir, *et al.*) - Ways and Means.

Information Source(s): Baltimore City; Allegany, Harford, Talbot, and Montgomery counties; Comptroller's Office; Maryland State Lottery Agency; Department of State Police; Department of Legislative Services

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