

Department of Legislative Services
 Maryland General Assembly
 2004 Session

FISCAL AND POLICY NOTE

House Bill 1257 (Delegate Arnick, *et al.*)
 Ways and Means

Video Lottery Terminals - Regulation - Location

This bill authorizes up to 10,000 video terminals consisting of 5,000 video lottery terminals (VLTs) and 5,000 Keno Video Terminals (KVTs). A maximum of three VLT licenses are to be competitively awarded with one license selected among Laurel Park and Pimlico and two licenses for all other applicants. A VLT facility can have a maximum of 1,500 VLTs. A maximum of five KVTs may be distributed to an entity that holds an alcoholic beverages license and currently offers Keno on the premises.

The bill takes effect June 1, 2004.

Fiscal Summary

State Effect: General fund revenues increase in FY 2005 and beyond due to application fees. General fund revenues decrease beginning in FY 2005 due to decreased lottery sales; future year losses increase with increased gaming implementation, totaling \$46.4 million in FY 2009. General fund expenditures increase in FY 2005 and beyond due to State Police expenditures. General fund expenditures decrease in FY 2005 and beyond due to the availability of revenues from the Education Trust Fund (ETF). Special fund revenues and expenditures increase for regulatory expenses, local aid, purse dedication, bred funds, gambling addiction treatment expenditures, and education beginning in FY 2005. **Appendix 1** shows the revenues and expenditures by fund in greater detail.

(\$ in millions)	FY 2005	FY 2006	FY 2007	FY 2008	FY 2009
GF Revenue	\$12.6	(\$7.1)	(\$31.7)	(\$44.6)	(\$46.4)
SF Revenue	29.1	78.3	331.1	458.2	469.2
GF Expenditure	(22.9)	(59.3)	(235.4)	(322.2)	(330.1)
SF Expenditure	30.7	82.1	338.9	466.0	476.9
Net Effect	\$33.8	\$48.3	\$196.0	\$269.8	\$276.0

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

Local Effect: Revenues for localities with gaming facilities would increase by approximately \$5.8 million in FY 2005, increasing to \$46.7 million at full implementation in FY 2009. Future year revenues represent increased operations and efficiency and revenues distributed from a nontrack VLT facility. 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

The bill authorizes a total of 10,000 video terminals in the State – 5,000 VLTs and 5,000 KVTs. A licensee can operate a maximum of 5 KVTs and 1,500 VLTs. Only one nontrack VLT facility can be located per county.

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 Agency is renamed as the Maryland Gaming Agency and will provide regulation and oversight of the VLT program.

Distribution of Video Terminal Proceeds

From the gross proceeds of VLTs, after pay out to players, proceeds are distributed as follows:

- 5% to the Maryland Gaming 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;
- 15% to the Purse Dedication Account (PDA) to enhance horse racing purses and to provide funds for the horse breeding industry;
- the operators will receive the amount stated on the successful bid, not to exceed 25%; and
- the remainder of the proceeds will be distributed to the ETF (minimum of 50%).

For the KVT locations, from the gross proceeds, after pay out to players, proceeds are distributed as follows:

- 15% to the local jurisdictions in which the keno lottery facilities operate;
- 25% to licensees;
- 60% to the ETF; and
- for KVL locations there is no allocation for administrative costs of the Maryland Gaming Agency.

Maryland Gaming Commission Authority and Duties

VLTs will be owned or leased by the Maryland Gaming Commission and under the control of the commission at all times. The State Lottery Commission is renamed as the Maryland Gaming Commission and the membership increases from five to nine.

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 and licensees.

VLT Licenses

Licenses must be obtained by operators, manufacturers, 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 licenses are subject to an application process that involves a State and national criminal history records check. All applicants for 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.

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.

Additional Requirements for Horse Track VLT Operation Licensees

None of the requirements in this section apply to the nontrack VLT facilities and only applies if the applicable horse track receives a VLT license.

If either the Preakness Stakes or Woodlawn Vase is transferred out of the State, the VLT operation license for Pimlico and Laurel Park will be revoked. In addition, the Maryland Million must be conducted annually at Laurel Park.

As a condition of licensure, 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 \$4 million of annual capital maintenance and improvements of the horse racing facilities (the Allegany track is required to make \$1.15 million in improvements annually).

Other Regulation of Video Lottery Operations and Consumer Protections

The bill prohibits a VLT operation licensee from offering food and beverages for a price that is lower than the prices in the county where the VLT facility is located.

The commission must adopt regulations to reduce or mitigate the effects of problem gambling, including provisions that provide for mandatory exclusion of career offenders from VLT facilities; procedures 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 to be given a record of spending levels to the extent that marketing measures that track customer spending are used. VLT licensees must ensure that intoxicated individuals and individuals aged 21 and under do not operate VLTs. The bill also requires the commission to adopt regulations requiring VLT licensees to submit specified annual financial reports.

Purse Dedication Account

The bill creates a Purse Dedication Account to which 15% of gross proceeds from the VLT facilities will be distributed. The money is distributed as follows:

- 89% to mile thoroughbred purses; 11% to the Maryland-bred Race Fund;

Education Trust Fund

The bill creates an ETF as a special, nonlapsing fund that will receive 60% of gross VLT revenues from the KVT facilities and an indeterminate share from the VLT facilities to fund the Bridge to Excellence in Public Schools Act of 2002 (Chapter 288 of 2002).

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.

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*.

State Revenues:

Application Fee Revenues

The bill requires the licensees of the three VLT facilities to pay an application fee of \$5 million. Application fees must be paid by October 1, 2004. These fees are to be distributed to the general fund. Assuming that three facilities opt to participate and pay their license fees by the required deadlines, general fund revenues would increase by up to \$15 million in fiscal 2005.

VLT Revenues

Three locations in the State may be licensed to operate a total of 5,000 VLTs, although each facility cannot have more than 1,500 VLTs. It is assumed that Pimlico or Laurel is awarded a license, as well as one other track and one nontrack location. It is assumed

that the win-per-day (WPD) at these facilities averages \$285, each facility begins operating at 50% of capacity and will reach full capacity one year later, and that the two tracks commence operations in May 2006 and the nontrack location in January 2007.

It is assumed that VLT operators will receive 25% of gross proceeds. To the extent that the successful bids accept less than 25%, State revenues will increase.

Distribution of Revenues

Exhibit 1 details the revenue distribution resulting from VLTs for fiscal 2006 through 2009.

Exhibit 1				
Distribution of VLT Revenues				
(\$ in millions)				
	<u>FY 2006</u>	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>
Total Annual Gross	\$26.0	\$284.4	\$453.5	\$468.1
ETF	13.00	142.59	229.47	237.33
Licensees	6.50	71.11	113.37	117.03
PDA	3.90	42.67	68.02	70.22
Local	1.30	14.22	22.67	23.41
MD Gaming Operations	1.30	13.86	19.94	20.13

Exhibit 2 lists the estimated revenues generated from KVTs. These estimates assume a WPD for each machine of \$85. This estimate is based on the average 2002 WPD for convenience VLTs in West Virginia that are distributed throughout the State and are adjusted for Maryland’s demographics. The regulations regarding the convenience West Virginia VLTs are similar to the ones proposed by the bill.

Exhibit 2
Keno Video Revenues
(\$ in millions)

	<u>FY 2005</u>	<u>FY 2006</u>	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>
Machines	1,250	2,500	5,000	5,000	5,000
Gross Revenues	\$38.8	\$77.6	\$155.1	\$155.1	\$155.1
Licensee	9.7	19.4	38.8	38.8	38.8
Local Jurisdictions	5.8	11.6	23.3	23.3	23.3
ETF	23.3	46.5	93.1	93.1	93.1
Keno Licensing Fees	*	*	*	*	*
Estimated Administrative Costs	1.6	3.9	7.8	7.8	7.8
State Net Effect	\$21.6	\$42.7	\$85.3	\$85.3	\$85.3

* Potential significant revenues, the amount will depend on number and amount of licenses fees.

Effect on Lottery Sales

The Department of Legislative Services (DLS) estimates that this expanded gaming, 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 authorization of 10,000 video terminals. **Exhibit 3** details the estimated decline in the 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 gaming implementation.

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

<u>FY 2005</u>	<u>FY 2006</u>	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>
\$2.4	\$7.1	\$31.6	\$44.6	\$46.4

The Lottery Agency estimates that lottery revenues would decline by \$6.5 million in fiscal 2005, \$27.8 million in fiscal 2006, \$30.5 million in fiscal 2007, and \$20.0 million in fiscal 2008 before rebounding in fiscal 2009 and beyond.

State Expenditures:

Compulsive Gambling Fund

Approximately \$1.8 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.

Administrative Expenditures

Maryland Gaming Agency

This agency is to receive 5% of VLT revenues in the first year and 4.3% thereafter. The bill does not provide for the agency to receive revenues from keno terminals to cover equivalent administrative expenses. It is assumed that the agency will require an appropriation of 4.3% of gross gaming revenues in year one and 5.0% in year two and thereafter of keno terminal revenues to cover administrative costs.

State Police

The Department of State Police estimates that it would incur increased general fund expenditures of approximately \$391,335 in fiscal 2005 to conduct background checks.

Purse Dedication Account

Exhibit 4 details the distribution from the PDA, for fiscal 2006 through 2009, assuming that the account is fully funded in each of those years.

Exhibit 4
Purse Dedication Account

<u>Purse Dedication Amount</u>	<u>FY 2006</u>	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>
<i>Thoroughbred</i>				
Purses	\$3,471,834	\$32,114,468	\$41,662,013	\$41,662,013
Bred Fund	<u>429,103</u>	<u>3,969,204</u>	<u>5,149,238</u>	<u>5,149,238</u>
Total Expenditures	\$3,650,938	\$35,833,672	\$46,561,250	\$46,561,250

Indirect Expenditures

In addition to 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. In addition, studies have indicated that convenience gambling (gambling located at many locations likely to attract mainly in-state residents) increases social costs as compared with destination-type gambling.

Local Fiscal Effect: Local revenues increase in both the local jurisdictions and counties in which KVTs and VLTs are located. Appendix 1 provides the total amount. Local expenditures would increase significantly in jurisdictions with VLT facilities.

Small Business Effect: Small businesses that operated the KVTs will benefit from gaming revenues. To the extent that VLT facilities purchase goods from local businesses that are small businesses, these small businesses would benefit. Other small businesses could be harmed by the 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: None.

Cross File: None.

Information Source(s): Department of State Police; Department of Health and Mental Hygiene; Department of Labor, Licensing, and Regulation; Department of Legislative Services

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Appendix 1
Summary of Fiscal Impact

	<u>2005</u>	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>
Gross Gaming Revenues	\$38,781,250	\$103,568,750	\$439,568,359	\$608,608,984	\$623,237,500
Distributions to Licensees	9,695,313	25,892,188	109,892,090	152,152,246	155,809,375
GF Revenues					
VLT application fees	15,000,000	0	0	0	0
Keno application fees	*	*	*	*	*
Lost Lottery Revenue	(2,419,358)	(7,100,639)	(31,658,193)	(44,618,844)	(46,384,835)
Total Known GF Revenues	12,580,642	(7,100,639)	(31,658,193)	(44,618,844)	(46,384,835)
SF Revenues and Expenditures					
Education Trust Fund (ETF)	23,268,750	59,540,625	235,660,767	322,547,648	330,408,038
Purse Dedication Account	-	3,900,938	42,666,504	68,022,598	70,216,875
Compulsive Gambling	-	585,000	1,462,500	1,755,000	1,755,000
Local Distributions	5,817,188	12,934,688	37,490,918	45,942,949	46,674,375
MD Gaming Expenses	-	1,300,313	13,858,080	19,943,543	20,128,838
Total Special Fund	29,085,938	78,261,563	331,138,770	458,211,738	469,183,125
GF Expenditures					
Education-Funded from ETF	(23,268,750)	(59,540,625)	(235,660,767)	(322,547,648)	(330,408,038)
Department of State Police	391,335	286,742	292,760	369,088	304,989
Total GF Expenditures	(22,877,415)	(59,253,883)	(235,368,007)	(322,178,560)	(330,103,049)
Nonbudgeted Keno Expenses	<u>1,628,813</u>	<u>3,878,125</u>	<u>7,756,250</u>	<u>7,756,250</u>	<u>7,756,250</u>
Net Effect	\$33,829,244	\$48,275,119	\$195,953,564	\$269,803,466	\$275,961,963