

Department of Legislative Services
 Maryland General Assembly
 2005 Session

FISCAL AND POLICY NOTE

House Bill 255 (The Speaker) (By Request – Administration)
 Ways and Means

Public Education Bridge to Excellence - Funding - Video Lottery Terminals

This Administration bill authorizes up to 15,500 video lottery terminals (VLTs) at six locations (four horse racing tracks and two 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 public school construction; and continues the current prohibition on additional forms of commercial gambling.

The bill takes effect June 1, 2005.

Fiscal Summary

State Effect: General fund revenues increase in FY 2006 and FY 2007 due to one-time application fees. General fund revenues decrease beginning in FY 2007 due to decreased lottery sales; future year losses increase with increased VLT implementation, totaling \$81 million in FY 2010. General fund expenditures decrease in FY 2008 and beyond due to the availability of revenues from the ETF. General fund expenditure increase beginning in FY 2006 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, and education beginning in FY 2007, except lottery and State Police expenditures which begin in FY 2006. **Appendix 1** shows the revenues and expenditures by fund in greater detail.

(\$ in millions)	FY 2006	FY 2007	FY 2008	FY 2009	FY 2010
GF Revenue	\$15.0	(\$3.8)	(\$49.8)	(\$77.1)	(\$81.4)
SF Revenue	0	71.8	634.9	951.9	975.6
GF Expenditure	0	.3	(330.9)	(584.2)	(605.6)
SF Expenditure	13.7	72.3	635.4	952.5	976.1
Net Effect	\$1.3	(\$4.6)	\$280.6	\$506.5	\$523.7

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 \$5.4 million in FY 2007, increasing to \$75.5 million at VLT full implementation in FY 2010. Future year revenues represent increased VLT operation and efficiency and revenues distributed from nontrack VLT facilities. Local expenditures increase significantly for local governments with VLT facilities.

Small Business Effect: A small business impact statement was not provided by the Administration in time for inclusion in this fiscal note. A revised fiscal note will be issued when the Administration's assessment becomes available.

Analysis

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

Video Lottery Terminals and Locations

The bill authorizes a total of 15,500 VLTs in the State – 3,500 VLTs each at Pimlico Race Course, Laurel Park, and Rosecroft Raceway; 1,000 at a race track built in Allegany County; and a total of 4,000 VLTs at two nontrack locations (emporia) to be determined by a commission created by this bill.

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 racetrack 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%);
- 4.75% to the local governments in which video lottery facilities are operating;
- 5.25% 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 5.95%);
- 39% to VLT operation licensees; and

- 46% to the ETF established under the bill.

For the two 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%);
- 4.75% to the county(s) in which the video lottery facilities operate;
- the operators will receive the amount stated on the bid proposals selected by the State Video Lottery Facility Commission; and
- the remainder of the proceeds will be distributed to the ETF.

Video Lottery Facility Location Commission

This bill creates a Video Lottery Facility Location Commission that will determine: (1) what entity(s) will operate the emporia; (2) the percent of operator VLT gross proceeds; (3) the emporium locations from among the following eligible locations: Prince George's, Howard, Baltimore, Harford, and Cecil counties, and Baltimore City; and (4) the distribution of the 4,000 VLTs between the two emporia. 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. In awarding the two nontrack VLT licenses, the commission is to consider various factors including the highest potential benefit to the State, the capital construction proposal, number of jobs created, licensee fees, and minority participation in the ownership group. Qualified bidders may submit bids according to the competitive sealed process established under Title 13 of the State Finance and Procurement Article. This bill does not specify a deadline for submitting bids or a decision deadline.

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.

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.

Additional Requirements for Horse Track VLT Operation Licensees

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

Applicants for horse track VLT licenses must submit a \$5 million application fee by October 1, 2005. The race track in Allegany County applicant has until October 1, 2006 to apply and pay an application fee of \$1.5 million.

In addition, applicants must also invest at least \$150 million in construction and related costs; provide at least 500 full-time jobs (the Allegany track is required to invest \$43 million and provide at least 150 jobs); and except for the Allegany track offer at least 15% of equity investment to minority investors if the licensee holds one license and 10% if the licensee holds two or more licenses.

As a condition of licensure, a track licensee must maintain the following number of live racing days:

- 220 days for the combined licenses at Laurel and Pimlico;
- 180 days for the Rosecroft license; and
- 21 days for the Allegany County 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 (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 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 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 (PDA) to which 5.25% of gross proceeds from the four track facilities will be distributed in the first year and 5.95% in the following years. Funds from the account are to be distributed as follows:

- from the proceeds at Laurel and Pimlico: 89% to mile thoroughbred purses; 11% to the Maryland-bred Race Fund;
- from the proceeds at Rosecroft: 89% to standardbred purses; 11% to the Standardbred Race Fund;
- from the proceeds at Allegany County, an amount to the thoroughbred industry and the standardbred industry prorated by the number of days of each type of racing at the track; and
- \$250,000 is to be dedicated annually 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 46% of gross VLT revenues from the four track facilities and an indeterminate share from the nontrack facilities to fund the Bridge to Excellence in Public Schools Act of 2002 (Chapter 288 of 2002). The bill mandates that in each fiscal year the Governor include at least \$50 million of the ETF received from VLT revenues for the GCEI and \$100 million for school construction and capital improvements.

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. 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 equity sales and facility construction. In addition, two studies must be conducted to evaluate the State's continued compliance with federal and constitutional requirements related to minority participation provisions.

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 Regional 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 Finance 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 2006 allowance includes no funding for the GCEI. HB 255 mandates in each fiscal year that the Governor include in the budget \$50 million of the ETF received from VLT revenues for the GCEI.

The bill also requires the Governor to include at least \$100 million in the annual budget from the ETF for school construction and capital improvements. 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. Increasing the funding by \$150 million annually, in addition to the \$100 million annually the State has already committed (the Governor's fiscal 2006 allowance includes \$157 million), for eight years would allow the State to meet the goal by fiscal 2013.

Although the Capital Debt Affordability Committee concluded that authorizing an additional \$1.2 billion in debt to provide the additional \$150 million per year would meet current affordability criteria, the committee recommended that other options, including alternative financing mechanisms, new revenue streams, and shifting capital projects, should be fully explored before increasing the bond authorization.

State Revenues:

Application Fee Revenues

The bill requires the licensees for Pimlico, Laurel, and Rosecroft to pay an application fee of \$5 million, and the licensee of the Allegany track to pay \$1.5 million. Application fees must be paid by October 1, 2005, except for the Allegany track, which has until October 1, 2006. These fees are to be distributed to the general fund. Assuming that all the tracks opt to participate and pay their license fees by the required deadlines, general fund revenues would increase by up to \$15 million in fiscal 2006 and by \$1.5 million in fiscal 2007. The nontrack facilities are not required to pay upfront fees, although they may opt to do so as part of their competitive bid.

VLT Revenues

Six locations in the State may be licensed to operate a total of 15,500 VLTs: 11,500 VLTs must be located at horse racing tracks and 4,000 VLTs must be located at two nontrack locations to be determined by the Location Commission. Pimlico, Laurel, and Rosecroft are authorized to operate up to 3,500 VLTs, and the Allegany County track is authorized to operate 1,000 VLTs.

As a result, total revenues generated – after payouts to winning players, but **before** any other distributions are made – could total approximately \$114.1 million in fiscal 2007, \$1.03 billion in fiscal 2008, \$1.55 billion in fiscal 2009, and approximately \$1.59 billion in fiscal 2010 and later.

Exhibit 1 details many of the important assumptions in these estimates. It is assumed that each facility begins operating at 50% of capacity and will reach full capacity one year later. An additional six-month delay due to the bid process is assumed for the emporia.

Exhibit 1 Assumed Start of Operations and Win-per-day

<u>Location</u>	<u>VLTs</u>	<u>WPD</u>	<u>Begin Operations</u>	<u>Full Capacity</u>	<u>Planning/ Zoning</u>	<u>Construction</u>
Pimlico	3,500	\$262	May 2007	May 2008	10 months	12 months
Laurel	3,500	\$276	May 2007	May 2008	10 months	12 months
Rosecroft	3,500	\$316	May 2007	May 2008	10 months	12 months
Allegany	1,000	\$225	January 2007	January 2008	8 months	10 months
Emporium 1	2,000	\$285	January 2008	January 2009	12 months	12 months
Emporium 2	2,000	\$285	January 2008	January 2009	12 months	12 months

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

Win-per-day estimates for the three central Maryland facilities 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 the two 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 two nontrack facilities are the average of the three central Maryland track facilities. To the extent that win-per-days are higher at the emporia, relative to the racetrack facilities, annual revenues to the ETF will be greater, and purse dedication amounts will be less.

It is assumed that nontrack VLT operators will receive 39% of gross proceeds – the same level provided under this bill to the track facilities. As a result, it is assumed that 51.25% of the gross proceeds from the two emporia will go to the ETF (51.95% in the second year and later of operations). To the extent that market forces cause the nontrack facilities to accept less than the 39% share that track operators receive, then the ETF revenues could be higher. For each 1% that the nontrack facilities underbid the amount received by horse track VLT facilities, the ETF revenues (at full implementation) would increase by approximately \$4.1 million annually.

Other Assumptions

- VLTs will operate 365 days a year, once operational.
- Virginia and Washington, DC do not authorize VLT gambling.
- West Virginia and Delaware do not expand VLT operations, either by adding additional VLT facilities or authorizing casino-style gambling.
- Pennsylvania does not expand gambling beyond VLT facilities authorized in 2004.

Distribution of Revenues

Exhibit 2 details the revenue distribution resulting from VLTs for fiscal 2007 through 2010.

Exhibit 2				
Distribution of VLT Revenues				
(\$ in Millions)				
	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY 2010</u>
ETF	\$52.5	\$481.2	\$734.5	\$755.9
Licensees	44.5	402.8	604.7	619.9
PDA	6.0	51.3	69.8	69.8
Local	5.4	49.1	73.6	75.5
Lottery Operations	<u>5.7</u>	<u>48.4</u>	<u>67.9</u>	<u>68.3</u>
Total Annual Gross	\$114.1	\$1,032.8	\$1,550.5	\$1,589.5

Exhibit 3 details the estimated revenue that will be generated at each facility for fiscal 2007 through 2010.

Exhibit 3
Estimated Revenues Generated by Facility
Fiscal 2007 – 2010
(\$ in Millions)

	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY 2010</u>
Pimlico	\$27.9	\$257.9	\$334.6	\$334.6
Laurel	29.4	272.2	353.1	353.1
Rosecroft	33.7	311.3	403.9	403.9
Allegany	23.1	74.4	82.1	82.1
Emporium 1	-	58.5	188.4	207.9
Emporium 2	-	58.5	188.4	207.9
Total	\$114.1	\$1,032.8	\$1,550.5	\$1,589.5

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 4** 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 4
Estimated Loss in General Fund Revenue
Due to Decreased State Lottery Sales
(\$ in Millions)

<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY 2010</u>
\$5.3	\$58.0	\$79.0	\$81.4

The Lottery Agency estimates that lottery revenues would decline by 1% in fiscal 2006, 5% in fiscal 2007, 3% in fiscal 2008, and 1% in fiscal 2009 before rebounding in fiscal 2010 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, horse race track VLT facilities must (1) create 1,650 jobs; (2) undertake \$493 million of one-time capital improvements and construction costs; and (3) spend \$13.2 million annually in capital improvements to the horseracing 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 \$493 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.

The emporia are not subject to minimum job or capital expenditures requirements. The amount of capital expenditures or jobs created by these facilities cannot be reliably

estimated. If the nontrack facilities are located at existing structures, capital expenditures can be expected to be significantly less than the expenditures at the track facilities.

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 5**.

Exhibit 5
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 to the movies which generate liquor and admissions and amusement 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 \$360 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 \$138 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, although Pennsylvania has authorized VLTs, the Pennsylvania Gaming Board has not determined the location of these facilities. The location of these facilities could impact the annual revenue “recaptured” by Maryland VLT facilities.

State Expenditures:

Administrative Expenditures

Lottery Agency

The Lottery Agency states that it will need 50 additional employees. The agency estimates a budget request of approximately \$13 million will be needed for fiscal 2006 to pay for start-up costs associated with VLT operations. Administrative costs for the State Lottery to operate video terminals would be approximately \$5.7 million in fiscal 2007. 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 horse track VLT facilities would be split equally between the PDA and the ETF. Additional gross proceeds as a result of lower than estimated agency administrative costs at nontrack VLT facilities would be distributed to the ETF.

Attorney General

The Office of the Attorney General would incur increased general fund expenditures of approximately \$259,600 in fiscal 2007 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 2006 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, 2005. MDOT advises that it will incur increased special fund expenditures of \$100,000 in order to complete 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, 2006 for the first study and by September 30, 2008 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 6**, State VLT revenues after operating costs 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), including \$50 million annually for the GCEI, and \$100 million annually for public school construction and capital improvements. Under Chapter 288 there are significant increases in education aid beginning with fiscal 2005. The GCEI statutory formula is phased in over five years, reaching full funding in fiscal 2010; however, current law does not mandate that the Governor include funding in the budget. The mandated ETF funding provides a portion of the full formula amount, as shown in Exhibit 6. It is assumed that the availability of the ETF revenues to fund the increase in education mandated by Chapter 288 will result in an equivalent decrease in general fund expenditures beginning in fiscal 2008.

Exhibit 6
Education Funding Provided by HB 255
Fiscal 2006 through 2010

	<u>FY 2006</u>	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY 2010</u>
Total ETF Funds		\$52.5	\$481.2	\$734.5	\$755.9
Bridge to Excellence Funding		\$0.0	\$331.2	\$584.5	\$605.9
School Construction		\$39.4	100.0	100.0	100.0
GCEI funding provided by HB 255	\$0.0	\$13.1	\$50.0	\$50.0	\$50.0
Total GCEI Statutory Formula Amount	53.6	71.1	92.2	108.8	128.8
HB 255 Percent of Total GCEI	0%	70%	54%	46%	39%

Fiscal 2007 ETF revenues are estimated to not be sufficient to fund the mandated amounts for the GCEI and school construction. It is assumed that the amount of ETF revenue will be prorated based on the amount specified for each. It is also assumed that although the bill mandates that the Governor include \$150 million in the budget for school construction and the GCEI, funding will be provided only to the extent of total revenues in the ETF. **Appendix 3** lists a breakdown of GCEI funding by jurisdiction provided by the bill in fiscal 2008 and beyond.

Infrastructure Costs

The State and local governments could also incur significant costs associated with infrastructure upgrades at each of the racetracks 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.

Purse Dedication Account

Exhibit 7 details the distribution from the PDA, for fiscal 2007 through 2010, assuming that the account is fully funded in each of those years.

Exhibit 7
Purse Dedication Account

<u>Purse Dedication Account</u>	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY 2010</u>
<i>Thoroughbred (Pimlico, Laurel)</i>				
Purses	\$2,677,597	\$25,481,802	\$36,415,325	\$36,415,325
Bred Fund	330,939	3,149,436	4,500,771	4,500,771
<i>Standardbred (Rosecroft)</i>				
Purses	1,572,565	16,485,728	21,386,891	21,386,891
Bred Fund	194,362	2,037,562	2,643,324	2,643,324
<i>To Be Allocated (Allegany)</i>				
Purses	1,079,238	3,733,364	4,348,929	4,348,929
Bred Fund	133,389	461,427	537,508	537,508
Total Purses	5,329,400	45,700,894	62,151,145	62,151,145
Total Bred Funds	<u>658,690</u>	<u>5,648,425</u>	<u>7,681,603</u>	<u>7,681,603</u>
Total Expenditures	\$5,988,091	\$51,349,320	\$69,832,747	\$69,832,747

The bill mandates that \$250,000 is to be spent annually on improving Maryland jockey health benefits. To pay for this, \$125,000 would be deducted annually from the standardbred and thoroughbred purses.

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. Revenues would increase for up to seven counties and one municipality due to the local distribution required by the bill as shown in **Exhibit 8**. Of VLT gross proceeds generated by Laurel, Pimlico, and Rosecroft collectively: Baltimore City and Prince George’s County are to receive 1.78% each; Anne Arundel County 0.7%; Howard County 0.33%; and Laurel 0.16%. For the Allegany track and emporia, 4.75% of gross proceeds will be distributed to the county in which they are located. Based on the assumed VLT-implementation schedule, local aid will total \$5.4 million in fiscal 2007, \$49.1 million in fiscal 2008, \$73.6 million in fiscal 2009, and \$75.5 million in fiscal 2010.

**Exhibit 8
Local Revenue Distributions**

<u>Location</u>	<u>Grantee</u>	<u>Percent Share</u>	<u>FY 2007</u>	<u>FY 2008</u>	<u>FY 2009</u>	<u>FY 2010</u>
Laurel/ Pimlico/ Rosecroft:	Anne Arundel	0.7%	\$636,729	\$5,889,739	\$7,640,742	\$7,640,742
	Howard	0.33%	300,172	2,776,591	3,602,064	3,602,064
	Laurel	0.16%	145,538	1,346,226	1,746,455	1,746,455
	Baltimore City	1.78%	1,619,110	14,976,765	19,429,316	19,429,316
	Prince George’s	1.78%	1,619,110	14,976,765	19,429,316	19,429,316
Allegany	Allegany	4.75%	1,097,139	3,535,225	3,900,938	3,900,938
Emporium 1	County	4.75%	-	2,777,599	8,950,042	9,875,908
Emporium 2	County	4.75%	-	<u>2,777,566</u>	<u>8,949,934</u>	<u>9,875,789</u>
Total			\$5,417,797	\$49,056,475	\$73,648,808	\$75,500,529

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 3,500 VLTs proposed at the three 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 the annual operating costs for public safety, sanitation, and transportation approximate \$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 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 as a result of the bill. This reflects hiring additional police and public works personnel as well as other operating costs. *Allegany, Anne Arundel, Baltimore, Howard, and Harford counties did not respond to a request to estimate local expenditures required as a result of this bill.*

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

Additional Information

Prior Introductions: None.

Cross File: SB 205 (The President) (By Request – Administration) – Budget and Taxation.

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

Fiscal Note History: First Reader - February 8, 2005
ncs/rhh

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Appendix 1

	<u>2006</u>	<u>2007</u>	<u>2008</u>	<u>2009</u>	<u>2010</u>
Gross VLT Revenues		\$114,058,900	\$1,032,767,900	\$1,550,501,200	\$1,589,484,700
Licensees		44,483,000	402,779,500	604,695,500	619,899,100
Special Fund Revenues					
Education Trust Fund		52,467,100	481,213,100	734,470,100	755,904,600
Purse Dedication Account		5,988,100	51,349,300	69,832,700	69,832,700
Compulsive Gambling		2,242,500	4,875,000	6,045,000	6,045,000
Local Distributions		5,417,800	49,056,500	73,648,800	75,500,500
Lottery VLT Administrative		5,702,900	48,369,500	67,854,100	68,347,800
Total SF Revenues		71,818,400	634,863,400	951,850,700	975,630,600
GF Revenues					
Application Fees	\$15,000,000	1,500,000	--	--	--
Lost Lottery Revenue		(5,344,900)	(49,848,200)	(77,082,500)	(81,391,200)
Total GF Revenues	15,000,000	(3,844,900)	(49,848,200)	(77,082,500)	(81,391,200)
Special Fund Expenditures					
Education Trust Fund		52,467,100*	481,213,100	734,470,100	755,904,600
Purse Dedication Account		5,988,100	51,349,300	69,832,700	69,832,700
Compulsive Gambling		2,242,500	4,875,000	6,045,000	6,045,000
Local Distributions		5,417,800	49,056,500	73,648,800	75,500,500
Lottery VLT Administrative	13,000,000	5,702,900	48,369,500	67,854,100	68,347,800
Transportation - Studies	100,000	50,000	50,000		
Total SF Expenditure	13,100,000	71,868,400	634,913,400	951,850,700	975,630,600
GF Expenditures					
Attorney General		259,600	274,000	289,300	305,600
State Police	639,400	462,800	472,500	599,300	492,100
Education - from ETF		--	(331,213,200)	(584,470,100)	(605,904,600)
Total GF Expenditures	639,400	722,400	(330,466,700)	(583,581,500)	(605,106,900)
Net Effect	\$1,260,600	(\$4,617,300)	\$280,568,600	\$506,499,000	\$523,715,700

*In fiscal 2007 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 these mandates only to the extent provided by the ETF and are pro-rated if ETF revenues are less than \$150 million.

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	\$1,589.48
Table Revenue (millions)	\$105.7	\$377.9	\$70.2	N/A
Estimated Direct State and Local Revenues	\$270.0	\$888.7	\$145.2	\$831.4
Estimated Tax Rate	31%	38%	28%	52%
Win per Day	\$230	\$395	\$201	\$281
Total Population	2.6 million	8.3 million	1.8 million	5.5 million
Population over age 21	1.8 million	5.8 million	1.3 million	3.8 million
Population over 21 per VLT	199	431	206	246
VLT Revenues per person over 21 years old	\$422	\$335	\$357	\$417
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 African American	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 2003 or fiscal 2004 for other locations, other data are from 2003.
Source: Missouri, Illinois, Indiana Gaming Commissions; U.S. Census Bureau

**Appendix 3
GCEI Expenditures
Mandated by HB 255**

<u>County</u>	<u>Total</u>
Allegany	\$0
Anne Arundel	3,294,169
Baltimore City	8,645,984
Baltimore	2,069,166
Calvert	948,129
Caroline	0
Carroll	1,026,004
Cecil	0
Charles	1,348,209
Dorchester	0
Frederick	2,491,403
Garrett	0
Harford	0
Howard	1,880,026
Kent	54,600
Montgomery	12,095,776
Prince George's	15,848,656
Queen Anne's	215,745
St. Mary's	82,134
Somerset	0
Talbot	0
Washington	0
Wicomico	0
Worcester	0
Total	\$50,000,000