

**Department of Legislative Services**  
 Maryland General Assembly  
 2007 Session

**FISCAL AND POLICY NOTE**

Senate Bill 541 (Senators Klausmeier and Stone)  
 Budget and Taxation

**Maryland Vessel Gaming Act**

This bill authorizes up to 15,500 video lottery terminals (VLTs) at 16 licensed gaming vessels subject to approval by the county in which the vessels plan to dock. It provides for one-time application fees and the distribution of VLT proceeds.

The bill takes effect June 1, 2007.

**Fiscal Summary**

**State Effect:** General fund revenues increase in FY 2008-2010 due to one-time application fees. General fund revenues decrease beginning in FY 2009 due to reduced lottery sales; future year losses mount with increased VLT implementation, totaling \$57.7 million in FY 2012. Special fund revenues and expenditures increase for agency administrative expenses, local aid, and the Bay Restoration Fund beginning in FY 2009, except administrative expenses which begin in FY 2008. **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	\$ .1	(\$3.8)	(\$27.7)	(\$51.9)	(\$57.7)
SF Revenue	0	11.9	80.2	144.2	155.3
SF Expenditure	.7	11.9	80.2	144.2	155.3
Net Effect	(\$.6)	(\$3.8)	(\$27.7)	(\$51.9)	(\$57.7)

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

**Local Effect:** Revenues for localities that grant approval to gaming vessels would increase significantly. Local expenditures could increase significantly for local governments with gaming vessels.

**Small Business Effect:** Meaningful.

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## **Analysis**

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

### *Distribution of VLT Tax*

Vessel gaming operators retain 80% of the proceeds of VLTs, after pay out to players. The bill imposes a tax of 20% on the proceeds of VLTs, of which the Comptroller is required to distribute the amount necessary to pay for administrative costs at the Department of Labor, Licensing, and Regulation (DLLR) and local and State law enforcement agencies. After these administrative expenses, the remaining proceeds are distributed:

- 50% to counties that are designated as the home docks of any gaming vessels. The amount distributed is to be used to “help provide an adequate education for children attending prekindergarten through grade 12 public schools;” and
- 50% to the Bay Restoration Fund.

### *State Commission on Vessel Gaming*

This bill creates a State Commission on Vessel Gaming within DLLR. The commission is composed of seven members appointed by the Governor with the advice and consent of the Senate. The Governor also appoints the chairman of the commission. The commission is required to meet at least once every three months. The Secretary of Labor, Licensing, and Regulation with approval of the Governor, is required to appoint an executive director. The duties of the executive director include (1) collecting taxes and fees imposed by the bill; (2) administering licensing requirements; and (3) issuing commission reports.

### *Commission Authority and Duties*

The commission has authority to issue subpoenas and conduct investigations. The commission is required to adopt regulations by April 1, 2008 that:

- establish minimum levels of insurance to be maintained by licensees;
- set standards for VLTs, gaming vessels, and facilities for gaming vessels; and
- provide for enforcement of the provisions of the bill.

The commission is required to coordinate with State and local law enforcement to enforce provisions of the bill. The enforcement costs of law enforcement agencies will be paid by a portion of VLT proceeds. All fees collected by the commission are deposited into the State's general fund.

### *County Approval Required*

The bill requires that gaming vessels must have approval from the county where the vessel intends to have its home dock. A county may also regulate the times at which VLT gaming can be conducted on the vessel and whether gaming can be conducted while docked or only when cruising on a waterway.

### *VLT Licenses and Fees*

Licenses must be obtained to operate VLTs, supply a gaming vessel, and operate a gaming vessel. Applicants must pay an application fee to the commission of \$5,000 for a license to supply a gaming vessel, \$25,000 for a license to operate a gaming vessel, and a fee set by regulation for a license to operate video lottery terminals. Additionally, an applicant for a license to operate a gaming vessel must pay an investigation fee of \$50,000. The applicant may be required to pay additional investigation costs, or have the fee partially refunded if investigation costs less than the amount of the fee.

An applicant to operate a gaming vessel is required to obtain a surety bond in the amount of \$200,000. An individual or business entity may only be licensed to operate one gaming vessel. The term of licenses is five years. At the end of the five-year term, the licensee may reapply for a license renewal of five years, with a renewal fee of \$5,000.

### *Other Regulation of Video Lottery Operations and Consumer Protections*

Gaming vessels are required to operate a cashless wagering system that can only be operated with a token, chip, or electronic card. Individuals under the age of 21 may not board a gaming vessel or participate in any gaming on a gaming vessel.

Gaming vessels are required to:

- have a capacity of at least 400 individuals;
- have applicable licenses from the U.S. Coast Guard;
- be accessible to individuals with disabilities;
- be fully registered and licensed with any other applicable laws;
- not be longer than 150 feet;

- not have overnight cabin accommodation; and
- meet any other qualifications specified by regulations adopted by the commission.

The bill also requires the commission to study the patterns of wagering and by December 31, 2007 make recommendations to the Governor and the General Assembly as to whether limits on wagering losses should be imposed.

**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*.

Chapter 428 of 2004 established the Bay Restoration Fund to be administered by the Maryland Water Quality Financing Administration within the Maryland Department of the Environment. The main goal of the fund is to provide grants to waste water treatment plant (WWTP) owners to reduce nutrient pollution to the Chesapeake Bay by upgrading the systems with enhanced nutrient removal (ENR) technology. As a revenue source for the fund, Chapter 428 established a bay restoration fee on users of wastewater facilities, septic systems, and sewage holding tanks. Priority for WWTP funding is given to major WWTPs (those with a design capacity of at least 500,000 gallons per day). Major facilities not owned by local governments, as well as minor facilities (those with a design capacity of less than 500,000 gallons per day), will be targeted for funding only after the 66 major locally-owned WWTPs are upgraded.

### **State Revenues:**

The Department of Legislative Services (DLS) estimates for revenues generated from VLTs under this bill are based on the following assumptions:

- The maximum number of vessels allowed under this bill (16) are ultimately licensed.

- All counties with licensed gaming vessels permit vessels to operate VLTs both while on the water and while at dock, as authorized by the bill.
- Four vessels apply for licenses in fiscal 2008, eight apply in fiscal 2009, and four apply in fiscal 2010.
- All vessels begin operating 12 months after approval for a license and reach full operation after one year of opening.
- Each gaming vessel operates an average of 700 VLTs. Although the bill authorizes up to 15,500 VLTs, an average of 968 per vessel, it is unclear whether the size restrictions placed on vessels in this bill (maximum 150 feet length) would allow for that many VLTs. The estimated capacity of 700 VLTs per vessel is based on figures from other states that currently operate riverboat casinos.
- Once in operation, gaming vessels average a win-per-day (WPD) of \$190 per VLTs.

Win-per-day estimates are based on previous estimates of the market for VLTs in Maryland and are adjusted by DLS to reflect the restrictions placed on the availability of VLT gaming on vessels by the bill, the total number of machines authorized, 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**.

#### *Assumptions About Gaming Operations in Other States*

- 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.

#### *Application Fee Revenues*

The bill requires applicants for a license to operate a gaming vessel to pay an application fee of \$25,000. These fees are to be distributed to the general fund. Given the assumptions enumerated above, general fund revenues would increase by \$100,000 in fiscal 2008, \$200,000 in fiscal 2009, and \$100,000 in fiscal 2010. License fees to supply a gaming vessel are \$5,000, and fees to operate VLTs are to be set by regulation. The amount of revenue generated from these fees cannot be estimated at this time, but it is not expected to substantially impact State revenues.

### *Distribution of Revenues*

Total VLT revenues generated – after payouts to winning players, but **before** any other distributions are made – could total approximately \$59.6 million in fiscal 2009, \$400.9 million in fiscal 2010, \$720.8 million in fiscal 2011, and \$776.7 million in fiscal 2012.

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

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	<u>FY 2009</u>	<u>FY 2010</u>	<u>FY 2011</u>	<u>FY 2012</u>
VLT Operators	\$47.7	\$320.7	\$576.7	\$621.4
State Expenses <sup>2</sup>	1.3	0.7	0.7	0.8
Bay Restoration Fund	5.3	39.7	71.7	77.3
Counties	5.3	39.7	71.7	77.3
<b>Total Annual Gross</b>	<b>\$59.6</b>	<b>\$400.9</b>	<b>\$720.8</b>	<b>\$776.7</b>

<sup>1</sup>Does not include any reimbursement of State and local law enforcement costs, which would increase the distribution to the State and counties and reduce the distribution to the Bay Restoration Fund.

<sup>2</sup>Fiscal 2008 expenditures are reflected in fiscal 2009 when revenues would first become available.

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### *Effect on Lottery Sales*

DLS estimates that VLTs, 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 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.

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**Exhibit 2**  
**Estimated Loss in General Fund Revenue**  
**Due to Decreased State Lottery Sales**  
**(\$ in Millions)**

<u><b>FY 2008</b></u>	<u><b>FY 2009</b></u>	<u><b>FY 2010</b></u>	<u><b>FY 2011</b></u>
\$4.0	\$27.8	\$51.9	\$57.7

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*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. Construction jobs associated with the construction of gaming vessels could bring dollars into the areas surrounding the gaming vessels, providing an economic boost to the local economy. New jobs would generate incomes which would be subject to the income tax – revenues that are not currently being generated. If these jobs are higher (lower) paying than 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**.

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**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

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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 a gaming vessel 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 slightly more than 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 four VLT facilities since November 2006 and has approved licenses for 11 additional facilities, which could impact the annual revenue “recaptured” by Maryland VLT facilities.

**State Expenditures:**

*Commission on Vessel Gaming*

Special fund expenditures could increase by an estimated \$665,311 in fiscal 2008, costs for which reflect the full year. This estimate reflects the costs of hiring an executive director, one attorney, one accountant, two investigators, and two support personnel to staff the new Commission on Vessel Gaming within the Department of Labor, Licensing, and Regulation, as well as supplies, equipment, and other operating expenses.

Positions	7
Salaries	\$305,858
Fringe Benefits	131,019
Other Operating Expenses	<u>228,374</u>
<b>Total FY 2008 Expenditure</b>	<b>\$665,311</b>

Future year expenditures reflect (1) full salaries with 4.5% annual increases and 3% employee turnover; and (2) 1% annual increases in ongoing operating expenses.

*Reimbursement to Law Enforcement*

Additional expenditures may be required to reimburse costs to State and local law enforcement agencies. Because the future location of gaming vessels is unknown, these costs cannot be reliably estimated at this time.

*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. These costs cannot be reliably estimated. For a more in-depth discussion about the possible social costs as a result of authorizing VLTs, consult the *Legislator's Guide to Video Lottery Terminal Gambling*.

**Local Fiscal Effect:** The bill provides that county governments where vessels are docked receive, after administrative expenses, 50% of VLT proceeds generated by a gaming vessel that docks in the county. The amount of revenue distributed to counties must be used to provide an adequate public school education for prekindergarten through grade 12. Exhibit 1 shows the estimated distribution of VLT revenues to counties in fiscal 2009 through 2012.

VLT facilities could have substantial impact on the local areas in which they are located and might necessitate additional local expenditures. The bill requires the reimbursement of local law enforcement costs associated with gaming vessels, which cannot be reliably estimated at this time.

**Small Business Impact:** To the extent that gaming vessels purchase goods from local small businesses, these businesses 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 wagering for other spending.

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### **Additional Information**

**Prior Introductions:** SB 785 of 2006, a similar bill, was scheduled for hearing in the Senate Budget and Taxation Committee but the hearing was cancelled.

**Cross File:** None.

**Information Source(s):** Comptroller's Office; Maryland Department of the Environment; Department of State Police; Department of Labor, Licensing, and Regulation; Department of Legislative Services

**Fiscal Note History:** First Reader - March 5, 2007  
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Analysis by: Nicholas M. Goedert

Direct Inquiries to:  
(410) 946-5510  
(301) 970-5510

## Appendix 1

	<u>2008</u>	<u>2009</u>	<u>2010</u>	<u>2011</u>	<u>2012</u>
<b>Gross VLT Revenues</b>	\$0	\$59,578,000	\$400,864,000	\$720,819,700	\$776,720,000
<b>Licensees (80%)</b>	\$0	47,662,400	320,691,200	576,655,760	621,376,000
<b>Special Fund Revenues<sup>1</sup> (20%)</b>					
Vessel Gaming Comm. Expenses	\$0	\$676,738	\$703,103	\$738,460	\$760,402
County Distributions	0	5,286,766	39,734,849	71,712,740	77,291,799
Bay Restoration Fund	0	5,286,766	39,734,849	71,712,740	77,291,799
<b>Total SF Revenues</b>	<b>\$0</b>	<b>\$11,250,270</b>	<b>\$80,172,800</b>	<b>\$144,163,940</b>	<b>\$155,344,000</b>
<b>GF Revenues</b>					
Application Fees	\$100,000	\$200,000	\$100,000	\$0	\$0
Lost Lottery Revenue		(3,984,904)	(27,817,139)	(51,894,898)	(57,736,100)
<b>Total GF Revenues</b>	<b>\$100,000</b>	<b>(\$3,784,904)</b>	<b>(\$27,817,139)</b>	<b>(\$51,894,898)</b>	<b>(\$57,736,100)</b>
<b>Special Fund Expenditures</b>					
Vessel Gaming Comm. Expenses	\$665,311	\$676,738	\$703,103	\$738,460	\$760,402
County Distributions	0	5,286,766	39,734,849	71,712,740	77,291,799
Bay Restoration Fund	0	5,286,766	39,734,849	71,712,740	77,291,799
<b>Total SF Expenditure</b>	<b>\$665,311</b>	<b>\$11,250,270</b>	<b>\$80,172,800</b>	<b>\$144,163,940</b>	<b>\$155,344,000</b>
<b>Net Effect</b>	<b>(\$565,311)</b>	<b>(\$3,784,904)</b>	<b>(\$27,817,139)</b>	<b>(\$51,894,898)</b>	<b>(\$57,736,100)</b>

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<sup>1</sup> Does not include any reimbursement of State and local law enforcement costs associated with gaming vessels. State and local reimbursements would have the effect of decreasing special fund revenues and expenditures by the Bay Restoration Fund.

**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	11,200
VLT Revenue (millions)	\$772.7	\$1,941.43	\$455.5	\$776.72
Table Revenue (millions)	\$105.7	\$377.9	\$70.2	N/A
Estimated Direct State and Local Revenues	\$270.0	\$888.7	\$145.2	\$155.34
Estimated Tax Rate	31%	38%	28%	20%
Win-per-day	\$230	\$395	\$201	\$190
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	3.9 million
Population over 21 per VLT	199	431	206	348
VLT Revenues per Person over 21 Years Old	\$422	\$335	\$357	\$201
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 fiscal 2012, other data are from 2005 or fiscal 2004.  
Source: Missouri, Illinois, Indiana Gaming Commissions; U.S. Census Bureau