

Department of Legislative Services
Maryland General Assembly
2010 Session

FISCAL AND POLICY NOTE

House Bill 1288
Ways and Means

(Delegate Weir)

Video Lottery Terminals - Increase in Number of Terminals and Licensees

This bill authorizes the Video Lottery Facility Location Commission (Location Commission) to award video lottery operation licenses throughout the State to qualified applicants. The bill limits the number of newly authorized video lottery terminals (VLTs) to four per licensed location and 5,000 total; maintaining the 15,000 VLT limit on the five VLT facility operation licenses currently authorized in the State. The bill repeals the limit on the number of VLT licenses that may be awarded by the Location Commission. The bill authorizes the Location Commission to replace up to four specified video gaming devices with an equal number of VLTs per specified licensed establishment. The bill requires the commission to adopt necessary regulations.

The bill's enactment is contingent on the passage of HB 1066 of 2010, a constitutional amendment, and its ratification by the voters of the State.

Fiscal Summary

State Effect: Special fund revenues may increase beginning in FY 2012 and beyond due to additional VLT revenues. General fund revenues from lottery sales may permanently decrease by a significant amount if 5,000 additional VLTs are operating in the State. General fund expenditures increase in FY 2012 and beyond due to lottery agency expenditures, offset by a decrease in general fund expenditures beginning in FY 2011 due to the availability of Education Trust Fund (ETF) revenues. Special fund revenues and expenditures may increase for the purposes specified by the VLT program, potentially beginning in FY 2012. Due to uncertainties, the total revenue generated by the bill cannot be reliably estimated. *For illustrative purposes only*, under one set of assumptions, net VLT revenues may increase by \$120 million annually once all of the VLTs authorized by the bill are awarded and operating.

Local Effect: Local revenues may increase beginning in FY 2011 from additional local impact grants distributed from VLTs. To the extent VLTs authorized by the bill replace machines upon which the local admissions and amusement tax is being paid, these local revenues may decrease. Local expenditures are not affected.

Small Business Effect: Potential meaningful.

Analysis

Bill Summary: The Location Commission may award video lottery operation licenses throughout the State to (1) a holder of a Class B or Class D alcoholic beverages license that offers, in the licensed establishment, a Keno-type game or a video gaming device operated for amusement or entertainment only; or (2) a nonprofit fraternal organization that holds an alcoholic beverage license. The commission is authorized to award a total of 5,000 VLTs and up to four per licensee in a licensed establishment. The commission may replace up to four amusement- or entertainment-only gaming devices per licensed establishment with an equal number of VLTs.

Current Law/Background: 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. Among the restrictions, the General Assembly may only authorize additional forms or expansion of commercial gaming after approval of a referendum by the majority of Maryland voters during a general election.

Chapter 4, which was contingent on ratification of Chapter 5, established the operational and regulatory framework for the VLT program. Under Chapter 4, VLT facility operation licenses are awarded by a Location Commission. The State Lottery Commission will oversee VLT operations and will own/lease the VLTs and a central monitor and control system. Chapter 4 allows for a maximum of 15,000 machines, 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. In addition, geographic parameters for each jurisdiction within which a VLT facility may be located are provided. The Location Commission may alter VLT allocations if warranted by an evaluation of market and other factors; however, no more than 4,750 VLTs may be placed at any one location.

The allocation of the gross VLT revenues, after payouts to bettors, is as follows:

- Small, Minority, and Women-owned Business Investment Account: 1.5% to a small, minority, and women-owned business investment account;
- State Lottery: 2.0% to the lottery for administrative costs, with other costs provided for in the annual State budget;
- Local Impact Grants: 5.5% to local governments where a video lottery facility is operating, 18.0% of which would go for 15 years (starting in fiscal 2012) to Baltimore City through the Pimlico Community Development Authority and to Prince George's County for the community surrounding Rosecroft (\$1 million annually);
- Horse Racing Industry: 7.0% to a purse dedication account to enhance horse racing purses and funds for the horse breeding industry, not to exceed \$100 million annually; and 2.5% for an eight-year period to a Racetrack Facility Redevelopment Account, not to exceed \$40 million annually;
- Licensee (Operator): 33.0% to video lottery operation licensees; and
- Education Trust Fund: the remainder (48.5 to 51.0%) to the Education Trust Fund.

Revenues accruing to the Education Trust Fund are to be used for the Bridge to Excellence in Public Schools Act funding (including the Geographic Cost of Education Index (GCEI), public school construction funding, and public higher education construction, including community colleges.

At the 2007 special session, the General Assembly approved legislation (Chapter 6) that imposed a 20% State admissions and amusement tax on the net receipts generated from the operation of electronic bingo and electronic tip jars operated for commercial purposes. The revenues accrue to the general fund. This provision took effect January 3, 2008. Chapter 661 (HB 193) of 2009 increased the State admissions and amusement tax rate from 20% to 30% and dedicates the increase to a special fund created by the bill: the Special Fund for Preservation of Cultural Arts in Maryland.

Chapter 474 (SB 959) of 2008 prohibited certain gaming machines licensed by local jurisdictions, primarily electronic bingo and tip jar machines, from operating after July 1, 2009. The law altered the definition of "slot machine" to include a machine that reads a game of chance and a machine that delivers a game of chance. The law also provides for exceptions for certain machines that are not considered slot machines:

- machines that award the user additional free games;

- machines that are arcade-type games that provide noncash prizes of minimal value; and
- paper pull tab tip jars and paper pull tab instant bingo tickets that must be opened manually as long as the machine does not electronically read the ticket, does not alert the user to winnings, or does not tabulate the winnings.

Personal electronic bingo machines are also excluded as long as the machine does not allow a person to play more than 54 cards at one time. State Lottery Commission machines that dispense lottery tickets and VLTs are also excluded. Chapter 661 (HB 193) of 2009 extended from July 1, 2009 to July 1, 2012, the termination date for operating specified electronic instant bingo machines that would otherwise be illegal under the law.

Local Gaming

Each county is responsible for regulating gaming activities conducted by civic and charitable organizations. There is no statewide reporting of gaming activities by civic and charitable organizations. Gaming licensees may use the proceeds of gaming activities for the benefit of their own organizations, but do not need to share them with other organizations. However, slot machine operators must use half of the proceeds from slot machines to benefit a charity. State gaming law requirements currently apply to 15 counties.

Facilities operating electronic bingo are located primarily in Allegany, Anne Arundel, and Calvert counties. Tip jar gaming, predominantly paper based, is conducted in several Western Maryland counties including Allegany, Garrett, and Washington. There are approximately 987 electronic bingo, tip jar, and other machines in Allegany, Anne Arundel, Calvert, St. Mary's, and Washington counties.

A 2006 Abell Foundation report on underground video gambling found between \$6.4 to \$15.3 million in lost local admissions and amusement tax revenue for fiscal 2005, due to underreporting of income from nearly 3,500 amusement devices in bars and other businesses in Baltimore City and Baltimore County, many of which had not been licensed by the jurisdiction. A subsequent report by the foundation notes that the Comptroller's Office, in coordination with Baltimore City has located over 100 machine owners who had not been paying the tax. An unknown number of these "gray" machines are in operation throughout the State, primarily in Baltimore City and Baltimore County.

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. Legislation enacted in 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 five 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.

Admissions and Amusement Tax

All counties (with the exception of Caroline County), Baltimore City, and most municipalities impose a local admissions and amusement tax. Each unit of local government sets its own single tax rate or range of rates. This rate is expressed as a percentage of gross receipts, up to a maximum rate of 10%.

Each unit of local government is authorized to classify different types of activities, and the rate of tax need not be the same for each type. An admissions and amusement tax may not be imposed in a municipality by a county if the municipality already imposes a similar tax or specifically exempts any gross receipts from the admissions and amusement tax. However, if a municipality does not levy a tax, the county tax, if any, applies within the municipality. The local admissions and amusement tax is further limited by the State sales and use tax.

The maximum tax rate on the gross receipts subject to admissions and amusement tax may not exceed 10%, except if the 6% State sales and use tax also applies to these receipts. In these cases, the total tax rate may not exceed 11%, thus the local admissions and amusement tax may not exceed 5%. This limitation on the local tax arises primarily on performances accompanied by some type of food service (dinner theaters, *etc.*).

The Comptroller collects the local (*i.e.*, county or municipal) admissions and amusement tax and remits payment back to the local jurisdictions on a quarterly basis. The Comptroller also collects the 30% State admissions and amusement tax, which is levied on net proceeds (*i.e.*, after cash and prizes are paid out). In general, the admissions and amusement tax applied by the local jurisdictions is a gross receipts tax. The notable exception is Anne Arundel County, which allows for the prizes and cash awards from the electronic bingo parlors to be subtracted out.

On January 18, 2008, the Comptroller promulgated updated regulations to address concerns regarding the terms “electronic bingo” and “electronic tip jars.” Pursuant to State regulations, an electronic bingo or electronic tip jar is a game played in an electronic or electro-mechanical device that contains predetermined winning and losing games and signals the issuance of a winning play. Examples include (but are not limited to):

- electronic devices utilizing paper bingo or tip jar tickets; and
- electronic devices utilizing computer chips that simulate paper bingo or tip jar tickets that, when played by a customer, determine the outcome of winning or losing that is not random or subject to change, but is based on a predetermined set of winning or losing numbers.

West Virginia VLTs

Limited numbers of VLTs (Limited Video Lottery, or LVL) are available at licensed West Virginia bars, clubs, and fraternal organizations. Licensed retail premises may operate up to five VLTs whereas eligible fraternal societies and veteran’s organizations may operate up to ten VLTs. As of June 30, 2009, 7,960 of the 9,000 maximum authorized were operating at over 1,600 licensed locations throughout the state. In fiscal 2009, West Virginia’s LVL gross income totaled \$412 million. Gross income from over 10,000 VLTs at four West Virginia racetracks totaled \$848 million in fiscal 2009. Since fiscal 2002, LVLs have generated on average \$294 million in revenue; a win-per-day average of \$115. South Dakota and Oregon also regulate and operate state-run LVL programs.

Alcohol Beverages Licenses

The Comptroller’s Office advises that approximately 3,000 organizations hold a Class B license and 1,000 hold a Class D license. In addition, approximately 200 fraternal organizations are eligible to hold an alcoholic beverages license.

State Revenues: The actual revenue increase, which cannot be reliably estimated at this time, depends on the total number of VLTs installed at eligible locations, the average

revenue generated by each VLT, and the impact these VLT would have on lottery sales and revenues generated by facilities currently authorized to operate VLTs.

However, *for illustrative purposes only*, based on a preliminary analysis of data on West Virginia LVL revenues, it is estimated that if the full amount of VLTs authorized by the bill is awarded, after payouts to winning players, but **before** any other distributions are made, net VLT revenues generated may increase by \$120 million at full implementation. This revenue increase reflects the net of increased revenues from VLTs authorized by the bill *minus* revenue losses resulting at the facilities currently authorized to operate VLTs.

Exhibit 1 shows the distribution of the increased net revenues resulting from the bill at full implementation.

Exhibit 1
VLT Net Revenue Increase
Full Implementation
(\$ millions)

Total Annual Revenues	\$120.0
Education Trust Fund	58.2
Licensees	39.6
Local Governments	6.6
Small, Minority, Woman-owned Businesses	1.8
Purse Dedication Account	8.4
Racetrack Renewal Account	3.0
Lottery Operations	2.4

Effect on Existing State Revenues

It is estimated that the revenue generated from VLTs authorized by the bill will reduce lottery sales in the same manner as revenue generated from the facilities currently authorized to operate VLTs. Accordingly, general fund revenues may decrease by \$5.0 million annually due to decreased lottery sales if the total number of VLTs proposed by the bill are awarded.

To the extent VLTs authorized by the bill replace machines upon which the State admissions and amusement tax is being paid, State admissions and amusements taxes may decrease.

Problem Gambling Fund

Under current law a person authorized to operate VLTs is required to pay a fee of \$425 per VLT, which is credited to the Problem Gambling Fund administered by the Department of Health and Mental Hygiene. The fund must be used to establish a 24-hour hotline, provide counseling for problem gamblers, and establish problem gambling prevention programs and other support services. If the commission authorizes the full amount of VLTs authorized by the bill, \$2.1 million annually will be paid to the fund.

State Expenditures:

State Lottery

Current law requires the State Lottery Commission to purchase or lease VLTs. Up to 5,000 newly authorized VLTs will need to be connected to a State-run central monitor and control system from 1,250 (assuming each location is awarded the maximum four VLTs) or more locations across the State. This will entail significant annual State Lottery Agency expenditures, to the extent that awardees do not directly cover either of these costs.

Education Expenditures

ETF is a nonlapsing, special fund to be used for continued funding of the Bridge to Excellence formulas and programs, including GCEI. The fund may also be used to support capital projects for public schools, public colleges and universities, and community colleges. In light of the substantial structural deficit currently forecasted through fiscal 2015, it is assumed that all of the available ETF proceeds generated by VLTs authorized by the bill are used to support operating programs and therefore offset general fund expenditures.

Local Revenues: Local revenues may increase by \$6.6 million annually once the full amount of VLTs are awarded and operating. The distribution of these revenues depends on which businesses are awarded licenses and cannot be reliably estimated.

To the extent VLTs authorized by the bill replace machines upon which the State admissions and amusement tax is being paid, State admissions and amusements taxes may decrease.

Small Business Effect: Small businesses that are awarded VLTs under the bill may benefit from a net increase in business revenues. A business awarded the maximum of number of VLTs may increase gross revenues (before payment of operating expenses and taxes) on average by about \$40,000 annually.

Additional Information

Prior Introductions: None.

Cross File: None.

Information Source(s): Comptroller's Office, Maryland State Lottery Agency,
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