

Department of Legislative Services
Maryland General Assembly
2012 Session

FISCAL AND POLICY NOTE

House Bill 928
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's enactment is contingent on the passage of HB 925 of 2012, a constitutional amendment, and its ratification by the voters of the State.

Fiscal Summary

State Effect: Special fund revenues may increase beginning in FY 2014 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 2014 and beyond due to lottery agency expenditures, offset by a decrease in general fund expenditures beginning in FY 2014 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 2014. 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 \$145.1 million annually once all of the VLTs authorized by the bill are awarded and operating.

Local Effect: Local revenues may increase beginning in FY 2014 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: Small businesses that are awarded VLTs under the bill may benefit from a net increase in business revenues.

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. The bill requires the commission to adopt necessary regulations.

Current Law/Background: Two VLT gambling bills passed during the 2007 special session – House Bill 4 (Chapter 5) and Senate Bill 3 (Chapter 4). Chapter 5 was a constitutional amendment approved by Maryland voters at the November 2008 general election authorizing 15,000 VLTs at five locations in the State. Chapter 4, which was contingent on ratification of Chapter 5, established the operational and regulatory framework for the authorized VLT program.

Under Chapter 4, VLT facility operation licenses are awarded by the Video Lottery Facility Location Commission (Location Commission). The State Lottery Commission oversees VLT operations and owns/leases VLTs and the central monitor and control system. A maximum of 15,000 VLTs are allowed, 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 1,000 VLTs in Allegany County. In addition, geographic parameters for each jurisdiction within which a VLT facility may be located are provided.

Under current law, except for the Allegany County location, gross VLT proceeds are distributed as follows:

- Business Investment – 1.5% to a small, minority, and woman-owned business investment account;
- Lottery Operations – 2% to the State lottery for administrative costs, with other costs provided for in the State budget;
- Local Impact Grants – 5.5% to local governments in which a video lottery facility is operating, 18% of which would go for 15 years (starting in fiscal 2012 and

ending in fiscal 2027) to Baltimore City through the Pimlico Community Development Authority and \$1 million annually to Prince George's County for the community surrounding Rosecroft;

- Purse Dedication Account – 7% to enhance horse racing purses and funds for the horse breeding industry, not to exceed \$100 million annually;
- Racetrack Facility Renewal Account – 2.5% for an eight-year period to RFRA, not to exceed \$40 million annually;
- Licensee (Operator) – no more than 33% to video lottery operation licensees; and
- Education Trust Fund (ETF) – remainder to ETF (48.5%-51.0%).

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.

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, except for the slot machines operated on the Eastern Shore. 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 at least one-half of the proceeds from slot machines to benefit a charity.

Generally, it is a misdemeanor crime to possess or operate a slot machine in Maryland. However, certain nonprofit organizations are authorized to operate slot machines in the following nine Eastern Shore counties: Caroline, Cecil, Dorchester, Kent, Queen Anne's, Somerset, Talbot, Wicomico, and Worcester. Nonprofit organizations must be located in the county for at least five years prior to the application for a license and be a fraternal, religious, or war veterans' organization, or be affiliated with a national fraternal organization for less than 5 years but have been located within an eligible county for at least 50 years before applying for a license. The Comptroller's Office must regulate the specified slot machines and charge a license fee to cover the costs of regulating the machines.

Facilities operating electronic bingo are located primarily in Anne Arundel and Calvert counties. Tip jar gaming, predominantly paper based, is conducted in several Western Maryland counties including Allegany, Garrett, and Washington. A 2006 Abell Foundation report on underground video gambling found between \$6.4 million and \$15.3 million in lost local admissions and amusement (A&A) tax revenue for fiscal 2005, due to underreporting of income from nearly 3,500 amusement devices in bars and

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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, 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.

Prohibited Gaming and Admissions and Amusement Tax

In *Chesapeake Amusements Inc. v. Riddle*, the Maryland Court of Appeals took up the issue of "whether a dispensing machine with a video screen that displays the contents of the tickets that it dispenses and emits a musical tone that signals when a winning ticket is being dispensed is a 'slot machine,'" as defined by Maryland law. The Court of Appeals found that the machine in question was not a slot machine. In response to this decision, Chapter 474 of 2008 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.

Chapter 474 also prohibited certain gaming machines licensed by local jurisdictions, primarily electronic bingo and tip jar machines, from operating after July 1, 2009. Chapter 661 of 2009 extended this termination date to July 1, 2012.

All counties (with the exception of Caroline County), Baltimore City, and most municipalities impose a local A&A 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%.

The Comptroller collects the local (*i.e.*, county or municipal) A&A tax and remits payment back to the local jurisdictions on a quarterly basis. In general, the A&A tax applied by 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 machines to be subtracted out before the tax is imposed. The Comptroller also collects the State A&A tax on electronic gaming machines, which is levied on net proceeds (*i.e.*, after cash and prizes are paid out). However, as noted above, the State A&A tax applies to machines that are not authorized to operate after July 1, 2012.

West Virginia VLTs

Limited numbers of VLTs (Limited Video Lottery, or LVL) are available at licensed West Virginia bars, clubs, and fraternal organizations. In fiscal 2011, 7,889 of the 9,000 maximum authorized were operating at over 1,600 licensed locations throughout the state. In fiscal 2011, LVL generated a total of \$396.5 million in revenue, a win-per-day of \$138. Also, gross income from over 10,000 VLTs at four West Virginia racetracks totaled \$727 million in fiscal 2011.

Alcohol Beverages Licenses

The Comptroller's Office advises that in fiscal 2011 approximately 3,300 organizations held a Class B license and 1,000 held a Class D license. In addition, approximately 280 fraternal organizations held an alcoholic beverages license in fiscal 2011.

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 an 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 \$145.1 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.

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 approximately \$5.5 million annually due to decreased lottery sales if the total number of VLTs proposed by the bill are awarded. With the expiration of machines authorized by Chapter 474 after fiscal 2012, no State A&A revenue loss is assumed from the bill.

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

Education Trust Fund	\$70.4
Licensees	47.9
Local Impact Grants	8.0
Business Investment	2.2
Purse Dedication Account	10.2
Racetrack Renewal	3.6
Lottery Operations	2.9
Total Annual Revenues	\$145.1

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, an additional \$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

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community colleges. In light of the substantial structural deficit currently forecasted, 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 from VLTs may increase by \$8.0 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. Local tax revenues will decrease to the extent that VLTs reduce paper gaming and other amusements subject to local admissions and amusement taxes.

Additional Information

Prior Introductions: HB 1288 of 2010 received an unfavorable report from the House Ways and Means Committee.

Cross File: None.

Information Source(s): Comptroller's Office, Maryland State Lottery Agency, Department of Legislative Services

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mc/rhh

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