

Department of Legislative Services
Maryland General Assembly
2014 Session

FISCAL AND POLICY NOTE

House Bill 535
Ways and Means

(Delegate Elliott, *et al.*)

Veterans' Organizations - Instant Ticket Lottery Machines - Use of Proceeds

This bill alters the allocation of proceeds from instant ticket lottery machines operated by veterans' organizations. A veterans' organization licensed to operate instant ticket lottery machines must use at least half of the net after-payout proceeds from its instant ticket lottery machines for the benefit of a charity and the remainder of the proceeds from the machines must be used to further the purposes of the veterans' organization. Proceeds from instant ticket lottery machines will no longer go to the State Lottery Fund. The bill eliminates the requirement that 10% of the remaining money in the State Lottery Fund from the proceeds of pull tab sales by licensed veterans' organizations be paid to the Maryland Veterans Trust Fund (MVTF) after June 30, 2014.

The bill takes effect July 1, 2014.

Fiscal Summary

State Effect: Minimal decrease in general fund and MVTF special fund revenues. General fund expenditures for the State Lottery and Gaming Control Agency (SLGCA) potentially increase to modify or terminate its contract with a vendor of pull tab machines.

Local Effect: None.

Small Business Effect: None.

Analysis

Current Law: Chapter 1 of the 2012 second special session authorized SLGCA to issue specified veterans' organizations a license for up to five instant ticket lottery (pull tab) machines. Veterans' organizations in counties on the Eastern Shore are not eligible.

A licensed veterans' organization must locate and operate its pull tab machines at its principal meeting hall in the county. After deductions for commissions and prize payouts, the proceeds go to the general fund. Beginning July 1, 2014, 10% of the proceeds will be distributed to MVTF. A licensed veterans' organization must purchase or lease the pull tab machines from SLGCA, but may not use receipts from the sale of pull tabs that would otherwise go to the general fund (via the State Lottery Fund) to purchase or lease the machines.

Maryland Veterans Trust Fund

Chapter 742 of 2009 established MVTF, which consists of gifts and grants received by the Maryland Department of Veterans Affairs (MDVA). Money in the fund may be used to make grants and loans to veterans and their families, support public and private programs that serve veterans in the State, or support the Charlotte Hall Veterans Home. Money in the fund may also be used to invest in general obligations of the State or other securities, pay for the cost of administering the fund, or support any other programs that the Secretary of Veterans Affairs considers appropriate. Money expended from the fund is supplemental to and is not intended to take the place of funding otherwise appropriated to MDVA.

Background: **Appendix – Local Gaming** provides detailed background on local gaming in Maryland.

The distribution of proceeds for instant ticket lottery machines under the bill follows the distribution of proceeds for slot machines operated by qualified organizations on the Eastern Shore rather than lottery proceeds, which pay a commission to vendors including veterans' organizations, and after other required allocations, distribute the remaining proceeds to the general fund.

SLGCA estimates approximately 150 veterans' organizations will operate up to 750 pull tab machines beginning in fiscal 2015. Under current law, in exchange for selling State lottery products, licensed agents earn a commission, currently set at 5.5% of gross lottery sales. Once the Baltimore City video lottery facility opens in September 2014, the commission increases to 6% of gross lottery sales. A licensed agent may receive a cashing fee of up to 3% of prizes paid for services rendered in cashing winning tickets. Additionally, the State Lottery and Gaming Control Commission may authorize bonuses

and incentives up to 0.5% of the gross sales to licensed agents. However, the Budget Reconciliation and Financing Act of 2014 proposes to decrease the commission to 5% of gross sales and increase the total of bonuses and incentives that a lottery agent may receive from 0.5% to 1% of the gross sales for the year for which the bonuses or incentives are awarded in fiscal 2015 and in subsequent years.

Under current law, veterans' organizations may receive 8.715% of gross revenues from pull tab machines (6% of gross sales and 3% of the payout to customers). Under a pending contract, the vendor receives 41.74% of the net proceeds, which the veterans' organizations must pay. SLGCA estimates the veterans' organizations receive 50% of net proceeds after the organizations pay the vendor for the costs of the pull tab machines. Under the bill, veterans' organizations receive 50% of the net proceeds, but SLGCA estimates the veterans' organizations receive less than 9% of net proceeds *after* paying the pull tab machine costs.

State Revenues: The impact on general fund and special fund revenues will depend on the number of war veterans' organizations that operate authorized pull tab machines, their location with respect to video lottery terminal facility locations, the actual payout rates on pull tabs that are offered, and the degree to which pull tab machines constitute a substitute for video lottery terminal gambling in the State. Although these exact impacts cannot be determined at this time, the bill decreases revenues for MVTF and the general fund by a minimal amount.

State Expenditures: SLGCA has approved a contract with a vendor of pull tab machines. Under the bill, SLGCA may incur potential significant costs if SLGCA has to modify or terminate the contract so that it is aligned with the bill's provisions.

Additional Information

Prior Introductions: HB 579 of 2013 received a hearing in the House Ways and Means Committee, but no further action was taken.

Cross File: None.

Information Source(s): Comptroller's Office, Maryland State Lottery and Gaming Control Agency, Maryland Department of Veterans Affairs, Department of Legislative Services

Fiscal Note History: First Reader - February 19, 2014
mc/rhh

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Appendix – Local Gaming

Eastern Shore Slot Machines

Generally, it is a misdemeanor crime to possess or operate a slot machine in Maryland. However, legislation was enacted in 1987, 2007, and 2011 authorizing certain nonprofit organizations to operate slot machines in the nine Eastern Shore counties: Caroline, Cecil, Dorchester, Kent, Queen Anne’s, Somerset, Talbot, Wicomico, and Worcester (except for a specified area within Ocean City).

Each county is responsible for regulating gaming activities conducted by civic and charitable organizations. 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. Chapter 645 of 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 5 years but have been located within an eligible county for at least 50 years before applying for a license. Pursuant to Chapter 315 of 2011, the Comptroller’s Office must regulate the specified slot machines and charge a license fee to cover the costs of regulating the machines.

A qualified 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 on the income of each machine and the disposition of these proceeds.

Exhibit 1 shows the slot machine “handle” (or amount bet) by county for 58 organizations in fiscal 2013. The total amount bet was \$52.6 million, 89% of which was returned to gamblers. The Comptroller’s Office assesses a \$50 license fee per slot machine to cover its regulatory costs.

Exhibit 1
Slot Machine Handle for Eastern Shore Counties
Fiscal 2013
(\$ in Millions)

<u>County</u>	<u>Slot Machines</u>	<u>Handle</u>
Caroline	15	\$2.1
Cecil	45	11.5
Dorchester	30	5.6
Kent	25	1.9
Queen Anne's	30	10.7
Somerset	20	1.5
Talbot	25	3.4
Wicomico	58	9.6
Worcester	33	6.1
Total	281	\$52.6

In reviewing past filings, the Department of Legislative Services (DLS) noted that several organizations were not in compliance with the 50% charity requirement or misclassified some contributions as charitable.

Paper Gaming

Paper gaming is a game of chance in which prizes are awarded, and the devices used to play the game are constructed of paper. The most common forms of paper gaming are punchboards, instant bingo, and tip jars. A punchboard is a square piece of wood or cardboard with dozens or hundreds of holes punched in it, each filled with a piece of paper with numbers or symbols printed on it. The holes are covered with foil or paper, and players pay for the right to punch one or more holes. If the numbers or symbols on their slips of paper match a winning combination, they receive a prize, either cash or another item. Tip jars dispense instant winning game tickets similar to scratch lottery games.

Paper gaming provides two sources of revenues to counties: the sale of paper gaming licenses and tickets to operators, and taxes on paper gaming sales. The State Lottery and Gaming Control Agency advises that paper gaming occurs in at least 15 Maryland counties and is most prevalent in Allegany, Frederick, Garrett, and Washington counties.

Electronic Gaming

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.

Facilities operating electronic bingo are located primarily in Anne Arundel and Calvert counties. An entity licensed to offer instant bingo under a commercial bingo license on July 1, 2007, or by a qualified nonprofit organization may continue to operate a game of instant bingo in the same manner using electronic machines, provided that:

- the machines were in operation for a one-year period ending December 31, 2007, or under a commercial bingo license on December 31, 2007;
- the entity does not operate more than the number of machines in operation on February 28, 2008; and
- the conduct of the gaming and operation of the machines are consistent with all other provisions of the Criminal Law Article.

Basic electronic pull tab dispensers are currently available at a cost ranging from about \$2,500 to \$5,000 each, and manual lock and key dispensers are available for as low as \$150. Price points on pull tab games typically range from 25 cents to \$2.00. Information from other states indicates a payout rate of approximately 66% on pull tabs, meaning that two-thirds of the amount bet is returned to gamblers (considerably lower than the average payout of about 89% for Eastern Shore slot machines).

Prohibited Gaming

In *Chesapeake Amusements Inc. v. Riddle* (2001), 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 of 2008 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, and Chapter 603 of 2012 made permanent the authority for certain existing qualified organizations and licensed commercial bingo licensees to operate electronic instant bingo machines that would otherwise be illegal under State law after July 1, 2012. Under Chapter 603, the State Lottery and Gaming Control Commission must regulate certain electronic gaming devices and determine if they are operating lawfully. A gaming device that is not compliant by January 1, 2013, is an illegal gaming device that may not legally operate in the State.

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 machines that dispense lottery tickets and video lottery terminals are also excluded.

Veterans’ Organizations

Chapter 1 of the second special session of 2012 authorizes the State Lottery and Gaming Control Agency to issue certain veterans’ organizations a license for up to five instant ticket lottery (pull tab) machines. Veterans’ organizations in counties on the Eastern Shore are not eligible. After deductions for commissions (to the veterans’ organizations) and prize payouts, the proceeds go to the State general fund. Beginning July 1, 2014, 10% of the proceeds will be distributed to the Maryland Veterans Trust Fund.