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BILL ANALYSIS

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House Bill 4609 (Substitute H-2 as passed by the House)
House Bill 4610 (Substitute H-3 as passed by the House)
House Bill 4611 (Substitute H-1 as passed by the House)
Sponsor: Representative Larry Julian (House Bill 4609)
Representative Jack D. Minore (House Bill 4610)
Representative Joe Hune (House Bill 4611)
House Committee: Agriculture and Resource Management
Senate Committee: Gaming and Casino Oversight

Date Completed: 10-20-03

CONTENT

House Bill 4609 (H-2) would amend the Horse Racing Law to do the following:

- Authorize the Racing Commissioner to issue racing theater licenses to race meeting licensees and licensed casinos, for off-track wagering on horse races in Michigan or out of State.
- Limit the total number of racing theater licenses to 15.
- Allow authorized race meeting licensees and licensed multijurisdictional hubs to conduct account wagering (wagering by telephone or other electronic means) on live or simulcast horse races.
- Allocate portions of licensees' commissions from account wagering and wagering at racing theaters to an Agricultural Enhancement Purse Pool and to breeders' awards.

House Bill 4610 (H-3) would amend the Lottery Act to:

- Allow the Lottery Bureau to implement and operate video lottery games at licensed race meetings.
- Allow a licensee to install up to 500 video lottery terminals (VLTs), and apply for permission to install more.
- Provide for the allocation of funds from video lottery games to the School Aid Fund, a proposed "Agricultural Enhancement Fund", and Detroit.
- Make it a felony to manipulate the payoff or outcome of video lottery games.

House Bill 4611 (H-1) would amend the Code of Criminal Procedure to include manipulating the outcome or payoff of video lottery games in the sentencing guidelines as a Class D felony against the public trust, subject to a statutory maximum of 10 years' imprisonment.

The bills are tie-barred to each other. House Bills 4909 (H-2) and 4610 (H-3) are described in more detail below.

House Bill 4609 (H-2)

Racing Theater Licensees

The bill would authorize the Racing Commissioner to issue up to 15 racing theater licenses. A racing theater license could be issued only to a race meeting licensee, a racing corporation (which two or more race meeting licensees could form for the operation of one or more racing theaters), or a person licensed to conduct casino gaming under the Michigan Gaming Control and Revenue Act. (A "racing theater" would be an enclosed facility where patrons could view off-track telecasting and engage in off-track wagering on the results of the telecast horse races.)

A racing theater licensee could conduct pari-mutual wagering by patrons on the results of horse races held in this State or, if approved by the Commissioner, on the results of horse races held in other states. A racing theater license would not entitle the licensee to conduct account wagering, and no other

method of betting, pool making, wagering, or gaming could be used or permitted at licensed racing theaters.

A racing theater could not be closer than 25 miles to a licensed racetrack or another racing theater unless all race meeting licensees conducting race meetings at the other track or the other racing theater licensee waived this restriction.

The bill would require a racing theater licensee to televise and conduct off-track wagering on all horse races held in this State for which a televised signal was available. The racing theater licensee would have to pay compensation (a percentage of the money wagered) to the race meeting licensee holding the race, for the off-track telecast and for the use of information about the race available from the race meeting licensee.

The Commissioner would have to audit racing theater operations, and forward to the licensee daily audit reports on each day's off-track wagering.

A racing theater licensee could not knowingly accept a wager from a person under 18 years old.

Account Wagering

The bill would define "account wagering" as "a form of pari-mutual wagering on a horse race in which a wager is placed on the horse race by telephone or other electronic means, including...the internet".

The Racing Commissioner could authorize a race meeting licensee to conduct account wagering or contract with one or more other persons to operate the licensee's account wagering. The Commissioner also could license one or more multijurisdictional wagering hubs to conduct account wagering in the State. ("Multijurisdictional hub" would mean a business conducted in this State and in at least one other state that conducts account wagering.)

To place an account wager in this State, an individual (at least 18 years old) would have to establish a wagering account with an authorized race meeting licensee or a licensed

multijurisdictional wagering hub. The bill would regulate the manner of making deposits to a wagering account, the placement and acceptance of account wagers, and the posting of credits to an account.

A race meeting licensee or multijurisdictional wagering hub that conducted account wagering by the internet or other electronic method would have to provide a full accounting and verification of the source of wagers made, in the form of a daily download to a database designated by the Commissioner.

An account wager would have to be included in the pari-mutual pool of one of the following:

- If the wager were on a live race, the race meeting licensee that conducted the race.
- If the wager were on a simulcast race, the appropriate race meeting licensee as determined by Section 18(3) (which governs the formation of pari-mutual pools for interstate and intertrack simulcasts).

Commission Distribution; Breaks

A race meeting licensee or multijurisdictional hub that conducted account wagering, or a racing theater licensee, would have to retain a commission equal to that allowed under Section 17 (which states that a race meeting licensee must retain 17% of all money wagered involving straight wagers; and up to 28% without Commissioner permission or up to 35% with Commissioner permission of all money wagered involving any form of multiple wager).

From its commission, the race meeting licensee, multijurisdictional hub, or racing theater licensee would have to pay the following:

- If the race wagered on were a live race held by the race meeting licensee, 43.1% of the commission to the Agricultural Enhancement Purse Pool and 6.9% for distribution to breeders' awards.
- If the race were simulcast, the State tax on wagering under the Law; the fee paid to the sending host track under Section 18; 34.5% of the balance to the Agricultural Enhancement Purse Pool; and 5.5% of the balance to breeders' awards. (Under Section 18, a host track may collect up to

3% of the total amount wagered on the simulcast race at the receiving track.)

In addition, the race meeting licensee, multijurisdictional hub, or racing theater licensee would have to pay all breaks as required by Section 17. (Under that section, a race meeting licensee must pay all breaks directly to the city or township in which the racetrack is located as a fee for police, fire, and traffic services at and near each race meeting.)

Agricultural Enhancement Purse Pool; Breeders' Awards

The bill would add Section 19b to provide for the distribution of money designated by law for deposit into the Agricultural Enhancement Purse Pool. All certified horsemen's organizations participating in the distribution of this money would have to select a depository as the recipient of this money. The escrow agent selected by the participating horsemen's organizations would have to distribute this money as described below.

One percent would be divided between all mixed breed purse pools. This amount would have to be at least \$1,200,001 for the first full calendar year in which the distribution was made. For each subsequent year, the amount would have to be at least the minimum amount for the previous year adjusted in proportion to the increase or decrease in the simulcast purse pool.

If no race meeting licensee were conducting thoroughbred racing in a city area, 55% of the balance of the Agricultural Enhancement Purse Pool money would have to go to thoroughbred purse pools, and 45% to standardbred purse pools. Of the money paid under the Lottery Act, 45% would have to be paid to thoroughbred purse pools, and 55% to standardbred purse pools.

If a race meeting licensee were conducting thoroughbred racing in a city area, the balance of the Agricultural Enhancement Purse Pool money would have to be distributed equally between thoroughbred and standardbred purse pools.

Of the money from any source designated for breeders' awards under Section 19b, 1% would have to be used for the payment of

mixed breed awards. The balance would be divided between standardbred breeders' awards and thoroughbred breeders' awards in the same proportion as the division of Agricultural Enhancement Purse Pool money.

Money distributed to a breed's purse pools or breeders' awards would have to be divided between all race meeting licensees holding races in which that breed participated, in proportion to the amount wagered on races of that breed conducted by a licensee compared with the amount wagered on races of that breed throughout the State in the previous year.

Sire Stakes Funds

Each year, up to 0.25% of all money wagered on live and simulcast horse races in Michigan would have to be placed in a special quarter horse sire stakes fund, and the same amount would have to be placed in a special American paint horse sire stakes fund. The entire amount of each fund would have to be used to provide purses for races run exclusively for two- and three-year-old Michigan sired quarter horses or two- and three-year-old Michigan sired American paint horses, as applicable, at licensed race meetings in this State.

House Bill 4610 (S-3)

Video Lottery Games

The bill would allow the Lottery Bureau to implement and operate video lottery games at licensed race meetings in this State. The Bureau would own and have primary responsibility for the control and regulation of a video lottery game or video lottery terminal. If approved by the Bureau, video lottery games could be conducted at a race meeting lawfully held on public property, other than the State fairgrounds in Wayne County.

"Video lottery game" would mean a Bureau-approved, electronically simulated game of chance that was displayed on a VLT. "Video lottery terminal" would mean a Bureau-approved and -owned interactive electronic terminal device that was connected to the central control system and used to play video lottery games authorized by the Bureau. "Central control system" would mean a computer or computer system provided to and controlled by the Bureau that communicated

with VLTs to retrieve information and activate and disable the terminals.

A manufacturer of VLTs could not sell, lease, or place a VLT in Michigan without the Bureau's approval. A manufacturer would have to obtain a permit to apply for approval of a VLT or associated equipment.

The Bureau could not grant a permit (to function as a manufacturer) or a license (authorization for a race meeting licensee to operate VLTs) unless the applicant met specific criteria. An applicant for an initial license would have to pay an application fee of \$1,000. A license or permit would be valid for one year and could be renewed.

A licensee or permit holder would be subject to requirements set forth in the bill. Among other things, a licensee would have to monitor VLTs to prevent access or play by a person who was under 21 or visibly intoxicated. A licensee could not allow players access to an automated teller machine in the area where video lottery games were played; accept a credit card or debit card from a player for the exchange or purchase of video lottery game credits or for a cash advance to play video lottery games; or extend credit, in any manner, to a player to enable him or her to play a video lottery game.

Number of Terminals

A license holder could install and operate a maximum of 500 VLTs at the racetrack where the licensee held race meetings. A licensee could apply to the Bureau for authorization to install and operate more than 500 terminals. If the Bureau determined that it was in the best interests of the licensee, the Bureau, and the citizens of this State, the Bureau could grant the license holder permission to install and operate additional VLTs.

Distribution of Video Lottery Income

A licensee would have to remit its gross terminal income to the Bureau by electronic transfer of funds on dates the Bureau established. The Bureau would have to deduct from the gross terminal income an amount sufficient to reimburse itself for administrative costs.

The Bureau would have to combine net terminal income from all licensees and distribute 40% to the State Treasurer, who would have to pay the following:

- One-third of the first \$90 million received each year to the School Aid Fund (SAF).
- One-third to the Agricultural Enhancement Fund.
- One-third to a city in this State with a population of at least 750,000.

Of the remaining balance of net terminal income, 15% would have to be distributed to the Agricultural Enhancement Fund, and 15% to the SAF. Of the balance, if the amount deposited into the SAF from State lottery games conducted as of May 22, 2003, and under the Michigan Gaming Control and Revenue Act decreased in a fiscal year after 2003-04 from the amount deposited into the School Aid Fund from those sources in fiscal year 2003-04, then an amount equal to the amount of the decrease would have to be deposited into the School Aid Fund.

The Bureau would have to distribute 42.5% of the net terminal income as commissions to race meeting licensees, in proportion to the percentage of the total amount wagered in video lottery games during the previous year that was wagered in games conducted at a licensee's racetrack. A race meeting licensee would have to pay 0.5% of the money received, up to \$1 million per year, to the local unit of government in which the racetrack was located.

The Bureau would have to distribute 15% of the net terminal income to the Agricultural Enhancement Purse Pool, and 2.5% to breeders' awards.

Agricultural Enhancement Fund

The bill would create the Agricultural Enhancement Fund within the State Treasury. Money in the Fund at the close of the fiscal year would remain in the Fund and would not lapse to the General Fund.

The Michigan Department of Agriculture (MDA) would have to spend money from the Fund, upon appropriation, for the purposes of enhancing the development of agriculture in this State, including the following:

- Support of value-added opportunities, including market development, export enhancement, quality and purity assurance, product development, packaging, and alternative energy development.
- Research and diagnostic capabilities for agricultural plants and animals.
- Environmental programs that provide incentives for on-farm practices or structures to reduce potential impacts on air, water, and soil.
- Rehabilitation programs for race horses.
- Farmland preservation.
- Agricultural production practices that efficiently use water in the production of feed, food, and fiber.
- Leadership development or educational programs that directly support production agriculture.
- Food security.

Penalty

Unless authorized by the Bureau, a person who intentionally manipulated the outcome, payoff, or operation of a video lottery game would be guilty of a felony punishable by up to 10 years' imprisonment, a minimum fine of \$10,000, or both.

Support Arrearage & Liability to the State

Under the Act, if a person who wins at least \$1,000 has a current liability to the State, including a delinquent account of money due to a court that has been assigned to the State for collection, or a support arrearage, the Bureau must apply the amount of the prize first to the liability to the State, next to a support arrearage, and then to an assigned delinquent account of money due to a court. The remainder of the prize, if any, is paid to the lottery winner.

Under the bill, the prize would be applied first to a support arrearage, next to the State liability, and then to the delinquent account of money owed to a court. Any remainder would be paid to the lottery winner.

MCL 431.302 et al. (H.B. 4609)
 432.3 et al. (H.B. 4610)
 777.14d (H.B. 4611)

Legislative Analyst: Julie Koval

FISCAL IMPACT

These bills would increase revenues both to the State School Aid Fund and to local units. The degree to which revenues would increase depends on a variety of unknown factors, such as how much video lottery terminals (VLTs) would reduce existing gaming under the lottery, American Indian casinos, the Detroit casinos, and other forms of gaming currently allowed; as well as how many machines would be operating, the prize payouts, and the amount of new gaming activity they would generate.

Video Lottery Terminals

Data from other states were examined to estimate the impact of these bills. However, none of the states that currently have VLTs matches Michigan's gaming landscape particularly well: Five of the states do not have casinos operated by Indian tribes or commercial interests; two of them offer VLTs only in bars or liquor-licensed establishments; none has more than four racetracks (while Michigan has seven); and few states have casinos near or in major urban areas. As a result, compared with Michigan, the VLTs in none of the other states have as much competition as would exist in Michigan. Among states that permit VLTs in racetracks only, the racetracks average approximately 1,200 machines per track, although each state's average varies widely. Generally, the more competition for gaming dollars (a higher number of racetracks and/or casinos, a wider proliferation of locations where VLTs can be placed, and/or more machines per track) and/or the more machines per capita, the lower the average daily win is per machine.

Using the averages for other states' experiences with VLTs and making adjustments to reflect the Michigan economy, a range for the amount of revenue that would be generated can be estimated given assumptions about how many machines would operate in this State. Video lottery terminals could be placed only at racetracks, of which there are seven currently operating in Michigan. House Bill 4610 (H-3) would limit each location to 500 machines unless the State Lottery Bureau authorized additional machines. The bill would not limit the number of additional machines the Bureau could authorize. Tables 1 and 2 present estimates

under two scenarios for VLT popularity using assumptions that tracks: 1) would be limited to 500 machines, and 2) would receive increases to allow an average of 2,000 machines per track.

Table 1 summarizes the estimated full-year impact, while Table 2 summarizes the estimated impact in FY 2003-04 assuming VLTs became operational on March 1, 2004. Under either scenario, the VLTs would not affect General Fund/General Purpose (GF/GP) revenue.

Table 1

Full-Year Estimated Net Fiscal Impact of VLTs at Racetracks (amounts in millions)						
	Total Net Revenue	General Fund	School Aid Fund	Commissions to Tracks	City of Detroit	Agricultural Interests
500 VLTs per Track						
Low popularity	\$66.7	\$0.0	\$5.2	\$31.0	\$7.9	\$22.5
High popularity	\$117.9	\$0.0	\$4.7	\$58.2	\$12.9	\$42.2
2,000 VLTs per Track						
Low popularity	\$171.5	\$0.0	\$8.2	\$83.7	\$19.0	\$60.7
High popularity	\$323.8	\$0.0	\$35.2	\$170.0	\$8.2	\$110.5

Table 2

FY 2003-04 Part-Year Estimated Net Fiscal Impact of VLTs at Racetracks (amounts in millions)						
	Total Net Revenue	General Fund	School Aid Fund	Commissions to Tracks	City of Detroit	Agricultural Interests
500 VLTs per Track						
Low popularity	\$22.7	\$0.0	\$1.1	\$10.7	\$2.4	\$7.7
High popularity	\$47.6	\$0.0	\$0.8	\$24.2	\$4.9	\$17.6
2,000 VLTs per Track						
Low popularity	\$66.5	\$0.0	\$1.5	\$33.7	\$6.9	\$24.4
High popularity	\$142.7	\$0.0	(\$3.1)	\$76.8	\$13.2	\$55.7

Under these assumptions, with 500 VLTs per track operating for a full year, the bill would be expected to increase School Aid Fund (SAF) revenue by between \$4.7 million and \$5.2 million, and City of Detroit revenue by between \$7.9 million and \$12.9 million. The seven local units where the tracks are located would receive between \$200,000 and \$300,000 each from the \$31.0 million to \$58.2 million that racetrack licensees would receive. Private agricultural interests would receive, through purse pools, grants and breeders' awards, between \$22.5 million and \$42.2 million.

If each track averaged 2,000 VLTs in operation for a full year, the bill would be expected to increase SAF revenue by between

\$8.2 million and \$35.2 million, and City of Detroit revenue by between \$8.2 million and \$19.0 million. The seven local units where the tracks are located would receive between \$400,000 and \$800,000 each from the \$83.7 million to \$170.0 million that racetrack licensees would receive. Private agricultural interests would receive between \$60.7 million and \$110.5 million.

However, the bill would not be effective for the entire fiscal year 2003-04. Assuming that VLTs could begin operating on March 1, 2004, with an average of 500 machines per track, the bill would increase SAF revenue by between \$0.8 million and \$1.1 million, and City of Detroit revenue by between \$2.4 million and \$4.9 million in FY 2003-04. The

seven local units in which the tracks are located would receive approximately \$100,000 from the \$10.7 million to \$24.2 million that racetrack licensees would receive during FY 2003-04. Private agricultural interests would receive, through purse pools, grants and breeders' awards, between \$7.7 million and \$17.6 million.

Assuming an average of 2,000 machines per track starting operation on March 1, 2004, the bill's impact on SAF revenue range from a net decline of \$3.1 million to a \$1.5 million increase in FY 2003-04, but would increase City of Detroit revenue by between \$6.9 million and \$13.2 million. The seven local units in which the tracks are located would receive \$200,000 to \$400,000 from the \$33.7 million to \$76.8 million that racetrack licensees would receive during FY 2003-04. Private agricultural interests would receive between \$24.4 million and \$55.7 million.

School Aid Fund "Hold Harmless" Provisions

House Bill 4610 (H-3) contains provisions to earmark additional money to the School Aid Fund should a specific subset of State lottery games and/or revenue from the State casino gaming tax decline from the FY 2003-04 level ("hold harmless" provisions). Any contribution to the SAF from VLTs would not be considered when computing the hold harmless amounts. Because of the formulas for distributing money and the manner in which the hold harmless payments would be computed, there would be a number of circumstances in which no hold harmless money would be distributed or it would be insufficient to hold the SAF fully harmless. There also would be circumstances in which the provisions would hold the SAF harmless for events unrelated to the addition of VLTs to racetracks.

First, because revenues to measure the hold harmless provisions are measured against FY 2003-04 final revenues, any loss to lottery and casino revenues experienced in FY 2003-04 would not create hold harmless payments; thus, the bill would not "hold harmless" against those losses. Second, the revenue to hold the SAF harmless would come from the residual created after the first \$90 million received by the State Treasurer was distributed. In years when the State Treasurer did not receive \$90 million, no money would be available for hold harmless payments to the SAF even though the SAF would have already experienced reductions

from lost lottery and casino revenue. Third, out of the residual from the \$90 million, the Agricultural Enhancement Fund and the SAF each would receive 15% before any money would be available to make hold harmless payments. In the example above, with highly popular VLTs at an average of 2,000 VLTs per track, \$70 million of residual would be available, of which \$10.5 million would be distributed to the SAF and the Agricultural Enhancement Fund each, leaving a balance of \$49.0 million. However, under this situation the SAF is forecasted to lose \$54.3 million in revenue from the lottery and the Detroit casinos--\$5.3 million more than would be available to hold the SAF harmless.

Despite the likely shortfalls in hold harmless payments, the bills also would trigger hold harmless payments when no loss was attributable to the operation of VLTs in the State or when the SAF might not have even taken a loss. Traditionally when the lottery has introduced new games, a portion of the activity on the new games is derived from decreased activity on other games. Because the bill would fix the games examined to create hold harmless payments, new games introduced by the lottery would reduce payments and trigger hold harmless payments. Similarly, SAF payments from the lottery vary from year-to-year and may decline for economic reasons unrelated to VLTs or even competition from casinos. School Aid Fund payments from the lottery have declined in every fiscal year since FY 1999-2000 and are estimated to decline in FY 2003-04 even without the introduction of VLTs. Lottery deposits to the SAF also declined four times in the 10 years prior to FY 1999-2000: in FY 1989-90, FY 1990-91, FY 1992-93, and FY 1995-96.

Account Wagering and Off-Track Betting

The amount of revenue generated from off-track betting (OTB) and account wagering under House Bill 4609 (H-2) would depend largely upon the amount of new gaming activity generated. Both options would essentially make it easier to place bets on races because bettors no longer would have to travel to an actual racetrack to place bets. Off-track betting parlors would have to be located 25 or more miles from any other OTB parlor or racetrack, although the bill provides an exception for this limitation, suggesting that much of the activity that would take place at OTB parlors could involve individuals who

would not otherwise travel to the racetrack to place bets. On the other hand, account wagering tends to provide incentives for individuals not to travel to either racetracks or OTB parlors because bettors would be allowed to place bets through the telephone, internet, and/or other communication media.

Using other states' experiences with OTB and account wagering, the effect on wagering can be estimated. The State School Aid and GF/GP Funds do not receive revenue from gaming activities at racetracks and would not receive revenue from OTB parlors or account wagering. The Agriculture Equine Industry Development Fund would receive 3.5% of the wagers, less prizes paid. Depending on the popularity of OTB parlors and account wagering, the bill would be expected to increase State revenue to the Agriculture Equine Industry Development Fund by between \$350,000 and \$600,000 in FY 2003-04, assuming a March 1, 2004, implementation date; and between \$1.2 million and \$1.6 million in FY 2004-05. Currently, the Fund receives about \$11.0 million from simulcast wagering at Michigan's seven licensed racetracks. This tax revenue is appropriated for administrative expenses, purse supplements, and owners/breeders' awards. Any new revenue would be available for the same purposes.

Penalties

The penalty provisions in House Bills 4610 (H-3) and 4611 (H-1) would have an indeterminate fiscal impact on State and local government.

There are no data to indicate how many offenders would be convicted of the proposed Class D crime of manipulating the outcome or payoff of a video lottery game. Offenders would receive a sentencing guidelines minimum sentence ranging from 0-6 months to 43-76 months. The fiscal impact for each offender would depend upon the sentence and the incarceration option chosen by the court. Local units would incur the costs, which vary by county, of incarceration in a local facility. For those placed on probation, the State would incur the cost of felony probation at an average annual cost of \$1,750, while the annual cost for those incarcerated in a State facility averages \$27,000.

Public libraries would benefit from any additional penal fine revenue raised due to the proposed changes.

This estimate is preliminary and will be revised as new information becomes available.

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This analysis was prepared by nonpartisan Senate staff for use by the Senate in its deliberations and does not constitute an official statement of legislative intent.