

COMMITTEE ON LEGISLATIVE RESEARCH  
OVERSIGHT DIVISION

**FISCAL NOTE**

L.R. No.: 1662-01  
Bill No.: SB 475  
Subject: Boards, Commissions, Committees, Councils; Fees; Gambling; Higher Education  
Department; Licenses - Miscellaneous; Lotteries.  
Type: Original  
Date: March 11, 2003

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**FISCAL SUMMARY**

<b>ESTIMATED NET EFFECT ON GENERAL REVENUE FUND</b>			
FUND AFFECTED	FY 2004	FY 2005	FY 2006
General Revenue	(Unknown)	(Unknown)	(Unknown)
<b>Total Estimated Net Effect on General Revenue Fund</b>	<b>(Unknown)</b>	<b>(Unknown)</b>	<b>(Unknown)</b>

<b>ESTIMATED NET EFFECT ON OTHER STATE FUNDS</b>			
FUND AFFECTED	FY 2004	FY 2005	FY 2006
Lottery Proceeds	\$0	\$0	\$0
Lottery Enterprise	\$1,846,091	\$2,409,789	\$3,119,228
Higher Education Trust	\$0	\$0	\$0
<b>Total Estimated Net Effect on Other State Funds</b>	<b>\$1,846,091</b>	<b>\$2,409,789</b>	<b>\$3,119,228</b>

Numbers within parentheses: ( ) indicate costs or losses.

This fiscal note contains 12 pages.

ESTIMATED NET EFFECT ON FEDERAL FUNDS			
FUND AFFECTED	FY 2004	FY 2005	FY 2006
None			
<b>Total Estimated Net Effect on <u>All</u> Federal Funds</b>	<b>\$0</b>	<b>\$0</b>	<b>\$0</b>

ESTIMATED NET EFFECT ON LOCAL FUNDS			
FUND AFFECTED	FY 2004	FY 2005	FY 2006
<b>Local Government *</b>	<b>\$2,497,500</b>	<b>\$12,065,000</b>	<b>\$19,135,000</b>

**\*Note: Local community colleges and other local political subdivisions could be appropriated some of the proceeds in the state Higher Education Trust Fund. However, local school districts would receive less funds as a result of the reduction in the Lottery Proceeds Fund.**

## FISCAL ANALYSIS

### ASSUMPTION

Officials from the **Department of Revenue, Office of the State Public Defender, Office of the State Courts Administrator** and the **Department of Public Safety - Division of Liquor Control** each assume no fiscal impact to their organization from this proposal.

Officials from the **Office of Prosecution Services** assumes that any cost resulting from this proposal could be absorbed within existing resources.

The **Department of Corrections (DOC)** did not respond to our request for fiscal impact. However, in response to a similar proposal from a previous year, DOC assumed no fiscal impact.

ASSUMPTION (continued)

Officials from the **Missouri Lottery Commission (LOT)** state this proposal would legalize video gaming machines in Missouri. LOT anticipates long-range sales losses for, at a minimum, the scratchers game, the pulltab game, and keno. They believe, based on their research in other states, that the pulltab game would not be able to compete in liquor-by-the-drink establishments with video gaming.

LOT states that the scratchers game, if it follows the experience of South Dakota, would lose approximately 50% of its base sales annually to video gaming by the third year. LOT estimates one-half of the sales loss experienced in South Dakota due to the fact that the games in Missouri may not be in direct competition as is the case in South Dakota convenience stores. Accordingly, LOT estimates that the scratchers game would lose approximately 25% of its base sales annually to video gaming by the third year. LOT assumes the pulltab game would also lose approximately 25% of base sales annually for three years with an unknown reduction thereafter. LOT assumes that keno would lose approximately 15% of current annual sales, and that future anticipated keno sales increases would not be realized.

LOT assumes this equates to a potential loss of \$219 million in gross sales of scratchers, a potential loss of \$36 million in gross sales of pulltabs, and a potential loss of \$54 million in Keno sales in the first three years, with unknown reductions in years thereafter. Losses to the state from the decrease in sales of scratchers, pulltab, and keno games is estimated to be \$13.1 million in FY 2004, \$29.5 million in FY 2005, and \$32.8 million in FY 2006.

**Oversight** assumes that transfers to replace the lost revenues, required by this proposal, would be made in the following state fiscal year.

LOT estimates that twenty-five (25) FTE would be required to administer this proposal. These would consist of one (1) Video Product Manager, one (1) Administrative Assistant, one (1) Inspector Manager, eight (8) VLT Field Inspectors, four (4) Computer Operator I's, three (3) Computer Operator II's, one (1) Communication Specialist, one (1) VLT Certifier Specialist, one (1) Systems Administrator, one (1) Programmer Analyst II, one (1) Game Accountant, one (1) Licensing Specialist II, and one (1) Security Specialist II. These positions were based upon staffing levels in the state of South Dakota and within the Missouri Lottery. Additional expenses include office equipment/supplies, travel expense, consulting and research, and 6 new vehicles. Costs for a central computer system have been estimated at \$1,900,000 in FY 2004, and \$79,000 each year thereafter.

ASSUMPTION (continued)

LOT estimates the revenue from licensing fees to be \$4,775,000 in FY 2004, \$3,575,000 in FY 2005 and \$4,325,000 in FY 2006. LOT also estimated revenues from the video lottery system as \$15,600,000 in FY 2004, \$41,600,000 in FY 2005 and \$52,000,000 in FY 2006.

Officials from LOT assume they would need assistance from the Missouri Highway Patrol (MHP) in two functions regarding this proposal;

1. Performing background checks on distributors, manufacturers, operators and vendors;  
and
2. Providing assistance during confiscation of illegal machines or gray area devices.

LOT estimates there would be a total of 115 distributors, manufacturers and operators to perform background checks upon, however, the extent of the background check to be performed has not yet been determined by the Lottery Commission. An additional 1,000 to 1,500 fingerprint background checks will be needed on potential retailers as well.

LOT states that the gray area devices are currently illegal, but local prosecutors tend not to prosecute these cases.

Officials from the **Department of Public Safety - Missouri Highway Patrol (MHP)** state that because they are unable to determine the number of machines that would be confiscated as a result of this legislation, the impact to their agency is an unknown cost to the General Revenue Fund. The MHP assumes that the number of background investigations performed through their Division of Drug and Crime Control would be minimal and would most likely be absorbed with existing FTE. If the number of investigations increases significantly, additional FTE would be required.

**Oversight** assumes the depth and extent of the background investigations required by the Lottery Commission will determine if the MHP can absorb these additional duties with existing resources.

Regarding confiscation and removal of illegal gaming machines, **Oversight** assumes that the number of illegal machines in Missouri is unknown but could be substantial. Oversight also assumes that at least some of the machine owners will voluntarily remove the illegal machines to comply with the law in lieu of facing a class D felony charge. Oversight also assumes the MHP's involvement in the physical confiscation and removal of the machine will consist of accompanying the LOT employees to the establishment and remaining at the location until the confiscation is complete. Oversight has reflected the potential cost to the MHP as an unknown

cost to the General Revenue Fund.

ASSUMPTION (continued)

Officials from the **Office of Secretary of State (SOS)** assume this proposal would create the video gaming machine network to generate revenue for higher education. The Missouri Lottery Commission may promulgate rules to implement this legislation. Based on experience with other divisions, the rules, regulations and forms issued by the Missouri Lottery Commission could require as many as 26 pages in the Code of State Regulations. For any given rule, roughly half again as many pages are published in the Missouri Register in the Code because cost statements, fiscal notes and the like are not repeated in Code. These costs are estimated. The estimated cost of a page in the Missouri Register is \$23.00. The estimated cost of a page in the Code of State Regulations is \$27.00. Costs due to this proposal are estimated to be \$1,599, however, the actual fiscal impact would be dependent upon the actual rule-making authority and may be more or less. Financial impact in subsequent fiscal years would depend entirely on the number, length, and frequency of the rules filed, amended, rescinded, or withdrawn. SOS does not anticipate the need for additional staff as a result of this proposal, however, the enactment of more than one similar proposal may, in the aggregate, necessitate additional staff.

**Oversight** assumes the SOS could absorb the costs of printing and distributing regulations related to this proposal. If multiple bills pass which require the printing and distribution of regulations at substantial costs, the SOS could request funding through the appropriation process. Any decisions to raise fees to defray costs would likely be made in subsequent fiscal years.

Officials from the **Department of Higher Education (DHE)** assume this proposal would establish the "Video Gaming Machine Network" and "Higher Education Trust Fund" for the deposit of revenues and interest generated by the network. The trust fund is for higher education purposes including maintenance and repair for public community colleges and four-year institutions, capital project bonding, increased funding to the Charles Gallagher Student Financial Assistance Program, increases to any other scholarship programs, and administration of the fund.

The DHE is unable to determine the fiscal impact of this proposal since the revenues expected from the "Video Gaming Machine Network" are unknown. The DHE assumes, however, that the "Video Gaming Machine Network" will increase the amount of state funding to higher education by providing new revenue through the "Higher Education Trust Fund." Due to current and proposed budget reductions, DHE further assumes additional administrative costs will be incurred to implement the provisions of this bill.

Officials from the **Office of the State Treasure (STO)** state the proposal, as it is written, requires their office to administer the new fund. With this language, the STO assumes the need for an additional

ASSUMPTION (continued)

FTE Accounting Analyst I (at \$27,444 annually). With fringe benefits and expenses and equipment, the STO assumes a total cost to the General Revenue Fund of roughly \$40,000 per year.

**Oversight** assumes the STO will be able to administer the new fund without an additional FTE.

Officials from the **Office of Administration - Budget and Planning (BAP)** assume this proposal would not result in any fiscal impact on their agency. However, the proposal would impact total state revenues and would also result in considerable general revenue fund costs.

BAP states that the proposal contains a provision that would help insulate the lottery proceeds fund (and programs that rely on the fund) from revenue losses resulting from the institution of video gambling as described in this proposal. However, the proposal contains no similar provision to protect the gaming proceeds for education fund (riverboat gambling) from such revenue losses. Since the types of games this bill would permit are currently available only on riverboats, it would appear that the proposal could reasonably be expected to result in a significant erosion in gaming proceeds for education fund receipts. Except for \$450,000 used for the school district bond program, all gaming proceeds for education fund revenues are used to fund the school foundation formula. Any reduction in that amount would have to be replaced with general revenue funds unless the school foundation formula was to be reduced. Likewise, the proposal could result in significant reductions in the amount of gaming commission fund revenue. Gaming commission fund net proceeds are the revenue source for the Veteran's Commission Capital Improvement Trust Fund, Missouri National Guard Trust Fund, Missouri College Guarantee Fund and the Early Childhood Development, Education and Care Fund. Thus, any significant downturn in gaming commission fund revenues would place the programs supported by these funds in jeopardy unless sufficient general revenue funds were available to make up the difference.

BAP also states that Article III, Section 39(b), subsection 3 of the Missouri Constitution requires that lottery net proceeds be transferred to the lottery proceeds fund, and that monies in the fund be appropriated for public institutions of elementary, secondary and higher education. Based on that requirement, BAP questions whether it would be constitutional to transfer revenue received by the Lottery Commission for video gaming to the higher education trust fund as required by

this proposal.

Officials from the **Missouri Gaming Commission (GAM)** assume the video gaming machine network would have a corresponding negative impact on the gaming taxes collected from Missouri's riverboats. GAM assumes that by FY 2006, up to 2,500 retailers would participate in the network, with an

ASSUMPTION (continued)

average of 4.5 machines at each location. Assuming an average win of \$46,800 per machine, GAM assumes in FY 2006 total gross revenue from these machines of \$526.5 million (2,500 x 4.5 x \$46,800). Assuming that 40 percent of this business is being taken away from Missouri's riverboats, then in FY 2006, \$210,600,000 (40% of \$526.5 million) in gross revenue is being diverted away. With an 18 percent state gaming tax rate, this would result in a loss to the Gaming Proceeds for Education Fund of \$37.9 million in FY 2006. GAM's estimates for FY 2004 and FY2005 are \$5,054,400 and \$23,587,200 respectively.

**Oversight** assumes the new Video Gaming Machine Network will not significantly impact the gaming boat revenues. Oversight assumes the new network could impact the revenues that are currently being collected by gray area devices, as defined in the proposal.

**Oversight** assumes the net amount of proceeds deposited into the Higher Education Trust Fund shall be appropriated and used for higher education purposes as described in Subsection 313.400.7 of this proposal. For purposes of the fiscal note, Oversight has shown the anticipated monies available in the Higher Education Trust Fund being distributed for the various purposes outlined in the proposal to the local level.

**Oversight** also assumes the reduction to the Lottery Proceeds Fund would result in a loss to the local elementary and secondary school districts in Missouri since proceeds from the fund are distributed to the schools.

FISCAL IMPACT - State Government

FY 2004  
(10 Mo.)

FY 2005

FY 2006

**GENERAL REVENUE**

<u>Costs</u> - to the Missouri Highway Patrol for assisting LOT in confiscation and removal of illegal gaming machines	(Unknown)	(Unknown)	(Unknown)
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<b>ESTIMATED NET EFFECT TO THE GENERAL REVENUE FUND</b>	<b><u>(UNKNOWN)</u></b>	<b><u>(UNKNOWN)</u></b>	<b><u>(UNKNOWN)</u></b>
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**LOTTERY PROCEEDS FUND**

<u>Income</u> - to Lottery Proceeds Fund			
Transfer from Higher Education Trust	\$0	\$13,102,500	\$29,535,000

<u>Savings</u> - less money to distribute to local school districts	\$13,102,500	\$16,432,500	\$3,330,000
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<u>Loss</u> - to Lottery Proceeds Fund			
Reduction in instant lottery revenues due to video gaming	(\$13,102,500)	(\$29,535,000)	(\$32,865,000)

<b>NET EFFECT TO LOTTERY PROCEEDS FUND</b>	<b><u>\$0</u></b>	<b><u>\$0</u></b>	<b><u>\$0</u></b>
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**LOTTERY ENTERPRISE FUND**

<u>Income</u> - Licensing Fees	<u>\$4,775,000</u>	<u>\$3,575,000</u>	<u>\$4,325,000</u>
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<u>Costs</u> - to the Lottery Commission			
Personal Service (25 FTE)	(\$465,322)	(\$620,429)	(\$651,451)

Benefits	(\$143,087)	(\$190,782)	(\$200,321)
Expense and Equipment	<u>(\$2,302,500)</u>	<u>(\$354,000)</u>	<u>(\$354,000)</u>
Total <u>Costs</u> to the Lottery Commission	<u>(\$2,910,909)</u>	<u>(\$1,165,211)</u>	<u>(\$1,205,772)</u>

<b>NET EFFECT TO THE LOTTERY ENTERPRISE FUND</b>	<b><u>\$1,846,091</u></b>	<b><u>\$2,409,789</u></b>	<b><u>\$3,119,228</u></b>
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**HIGHER EDUCATION TRUST  
 FUND**

<u>Income</u> - Video lottery revenues	\$15,600,000	\$41,600,000	\$52,000,000
<u>Costs</u> - Transfer to Lottery Proceeds Fund	\$0	(\$13,102,500)	(\$29,535,000)
<u>Costs</u> - capital improvements to higher education facilities and grants for student education at the local level	<u>(\$15,600,000)</u>	<u>(\$28,497,500)</u>	<u>(\$22,465,000)</u>

<b>NET EFFECT ON HIGHER EDUCATION TRUST FUND</b>	<b><u>\$0</u></b>	<b><u>\$0</u></b>	<b><u>\$0</u></b>
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<u>FISCAL IMPACT - Local Government</u>	FY 2004 (10 Mo.)	FY 2005	FY 2006
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<u>Income</u> - proceeds from the Higher Education Fund for capital improvements to higher education facilities and for student grants.	\$15,600,000	\$28,497,500	\$22,465,000
<u>Loss to local school districts</u> - less money distributed from Lottery Proceeds Fund	<u>(\$13,102,500)</u>	<u>(\$16,432,500)</u>	<u>(\$3,330,000)</u>

<b>ESTIMATED NET EFFECT TO LOCAL POLITICAL SUBDIVISIONS*</b>	<b><u>\$2,497,500</u></b>	<b><u>\$12,065,000</u></b>	<b><u>\$19,135,000</u></b>
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**\*Note: Local community colleges and other local political subdivisions could be appropriated some of the proceeds in the state Higher Education Trust Fund. However, local school districts would receive less funds as a result of the reduction in the Lottery Proceeds Fund.**

### FISCAL IMPACT - Small Business

A fiscal impact to small businesses qualified to host video gaming machines would be expected as a result of this proposal.

### DESCRIPTION

This proposal authorizes the Missouri Lottery Commission to create a statewide "Video Gaming Machine Network". Certain types of video gambling machines are authorized in licensed locations. The machines will be electronically linked to a main computer which will audit the functioning of the devices and provide transfers of funds to the machines.

The payback value of one credit wagered, determined over time, shall be a minimum of sixty percent but shall not exceed a maximum of eighty percent.

Revenues generated by the "Video Gaming Machine Network" will be placed in the "Higher Education Trust Fund", also created by this proposal, for the purpose of creating reserves for capital improvements to higher education facilities and providing grants for student education. A portion of this fund shall offset any decline in lottery sales.

A license is required for manufacturers, distributors and operators of such video games as well as for each machine and each premises containing the machines. Licensed distributors must have at least two years experience with distribution of video gaming machines. Licensed operators, who place machines in licensed premises, must have at least two years experience with operating video gaming machines.

Licensed premises include those where the sale and consumption of alcohol is permitted and truck stops that meet a threshold of 250,000 gallons of petroleum sold in each of the prior two years, as well as other locations approved by the commission. No license issued to a licensee shall be transferrable without the consent of the commission. A licensed premise shall provide the operator a surety bond of a certain amount not less than five thousand dollars.

A licensed premise may receive a maximum of two machines for the first year. After one year the commission may authorize up to two additional machines per year, not to exceed fifteen total machines.

The Director of the Lottery Commission shall set administrative rules for licensing of machine locations, distributors, manufacturers, and parts suppliers. The Commission will contract with these licensed entities on an annual basis.

Tampering with games or machines is a Class D felony. After the effective date of this proposal, it shall be illegal to operate any video device that can simulate a game played on a licensed video gaming machine.

DESCRIPTION (continued)

This legislation is not federally mandated, would not duplicate any other program and would not require additional capital improvements or rental space.

SOURCES OF INFORMATION

Department of Higher Education  
Missouri Gaming Commission  
Department of Revenue  
Department of Public Safety  
    Liquor Control  
    Highway Patrol  
Office of the Secretary of State  
Missouri Lottery Commission  
Office of Administration  
Office of the State Public Defender  
Office of Prosecution Services  
Office of the State Courts Administrator  
Office of the State Treasurer

**NOT RESPONDING:      Department of Corrections**

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A handwritten signature in black ink, reading "Mickey Wilson". The signature is written in a cursive, flowing style.

MICKEY WILSON, CPA  
DIRECTOR  
MARCH 11, 2003