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February 12, 2018

The Honorable John Barker, Chairperson
House Committee on Federal and State Affairs
Statehouse, Room 285-N
Topeka, Kansas 66612

Dear Representative Barker:

SUBJECT: Fiscal Note for HB 2545 by House Committee on Federal and State Affairs

In accordance with KSA 75-3715a, the following fiscal note concerning HB 2545 is respectfully submitted to your committee.

HB 2545 would amend the Kansas Expanded Lottery Act. First, the bill would allow the voters of Sedgwick County to file a petition with the Sedgwick County Election Office to hold a special election to allow the Kansas Lottery to operate electronic gaming machines at a parimutuel racetrack facility located in Sedgwick County. The bill would require the signatures of at least 5,000 qualified voters in Sedgwick County and would require the special election to occur within 120 days after the petition has been certified. If the voters of the special election approve the ballot measure, then the Executive Director of the Kansas Lottery would be authorized to enter into a contract with Wichita Greyhound Park to operate electronic gaming machines at that facility. The bill would also require gaming facility managers to pay for the gaming related expenses of the Kansas Lottery. It would make other technical corrections to the Kansas Expanded Lottery Act.

The bill would allow the Attorney General to file an action in the Kansas Supreme Court within 90 days from the effective date of the bill to determine if allowing a revote in Sedgwick County would be viewed as an expansion of gaming that is prohibited under the Kansas Expanded Lottery Act. The bill would require a signed contract between the Kansas Lottery and a racetrack gaming facility manager to place electronic gaming machines at the parimutuel racetrack and the issuing of a final order from the Supreme Court before a breach of contract lawsuit could be filed for violating the current state prohibition from designating additional areas of the state where gaming facilities are authorized until July 1, 2032. If a racetrack gaming facility is authorized in a gaming zone, then the bill would only let the casino manager in the same gaming zone to make a claim that the contract authorizing the racetrack gaming facility violates the law. The casino managers would then have 60 days after the final order or after a racetrack gaming facility contract is executed to file a legal action in Shawnee County District Court to determine if the contracts with the parimutuel racetracks are in violation of the Kansas Expanded Lottery Act or create a material breach of the casino manager's contract with the Kansas Lottery. The bill would only

allow the casino manager of the south central gaming zone to make a claim based on the Sedgwick County revote. Monetary damages awarded could not exceed an amount equal to the privilege fee paid by the facility manager plus accrued interest.

The bill would require a racetrack gaming facility manager to submit a letter of credit in the total amount equal to the privilege fee paid by the casino managers plus interest. If the court finds the racetrack gaming facility management contract violates state law that requires repayment of the casino manager privilege fees plus interest, the bill requires the Kansas Lottery to reimburse the racetrack gaming facility manager line of credit no less than 50.0 percent of the amount of Expanded Lottery Act Revenues Fund revenue generated from the racetrack gaming facility. If the court finds the racetrack gaming facility management contract does not violate state law and does not require repayment of the casino manager privilege fees plus interest, then the Kansas Lottery would cancel the letter of credit. The bill creates the Privilege Fee Repayment Fund to be administered by the Kansas Lottery. Expenditures from the fund will be for repayment of the privilege fees, including accrued interest. The bill creates the Racetrack Gaming Facility Manager Repayment Fund to be administered by the Kansas Lottery. Expenditures from the fund will be for reimbursement to the racetrack gaming facility manager for the letter of credit issued.

Current law allows for the first 2,200 electronic gaming machines at racetrack gaming facilities to be allocated and then a bidding process to place the remaining 600 machines occurs at a later date. The current bidding process allows existing casino managers to bid to prevent the placement of additional machines at racetrack gaming facilities. The bill removes the bidding process on the 600 machines and would allow the Kansas Lottery to allocate the entire 2,800 authorized electronic gaming machines to be placed at racetrack gaming facilities; however, each racetrack gaming facility would be required to have at least 400 machines. Each horse or greyhound racetrack would be required to conduct a minimum number of races in order to operate electronic gaming machines.

The bill would change the distribution of net electronic gaming machine revenue from the racetrack gaming facility located in the northeast gaming zone that operates parimutuel horse racing by increasing the amount of revenue distributed to the racetrack gaming facility manager from 25.0 percent to 66.5 percent in the first and second year of operation, 63.5 percent in the third and fourth year of operation, and 59.5 percent in the fifth year and future years of operation. The amount of revenue that goes to the Live Horse Racing Purse Supplement Fund would remain at 7.0 percent in the first and second year of operation and be increased to 10.0 percent in the third and fourth year of operation and 14.0 percent in the fifth year and future years of operation. The amount of revenue that goes to the Kansas Horse Fair Racing Benefit Fund would be increased from 1.0 percent to 2.0 percent. To balance out these increases, a corresponding reduction in revenues is in the bill. The state's share in the Expanded Lottery Act Revenues Fund (ELARF) would be reduced from 40.0 to 22.0 percent; the current 3.0 percent share that is shared by the city and county would be reduced to 2.0 percent; the share going to the Problem Gambling and Addictions Grant Fund would be reduced from 2.0 percent to 0.5 percent; the 7.0 percent share going to the Live Greyhound Racing Purse Supplement Fund would be eliminated; and the 15.0 percent share of gaming revenues that is to be used for gaming expenses would also be eliminated. Under current law, the 15.0 percent share of revenues can be used for any gaming expenses, subject to the agreement between the Kansas Lottery and the facility manager.

The bill would change the distribution of net electronic gaming machine revenue from racetrack gaming facilities located in the south central gaming zone that operates parimutuel greyhound racing by increasing the amount of revenue distributed to racetrack gaming facility managers from 25.0 percent to 68.4 percent. The bill would also create the Kansas Horse Council Fund which would require 0.1 percent of the revenues collected in the southeast gaming zone for the development, promotion, and representation of the equine industry in Kansas. To balance out these increases, a corresponding reduction in revenues is in the bill. The state's share in the ELARF would be reduced from 40.0 to 22.0 percent; the share going to cities and counties would be reduced from 3.0 percent to 2.0 percent; the share going to the Problem Gambling and Addictions Grant Fund would be reduced from 2.0 percent to 0.5 percent; the 1.0 percent share going to the Kansas Horse Fair Racing Benefit Fund would be eliminated; the 7.0 percent going to the Live Horse Racing Purse Supplement Fund would be eliminated; and the 15.0 percent share of gaming revenues would be eliminated. The share going to the Live Greyhound Racing Purse Supplement would remain unchanged at 7.0 percent.

The bill would change the distribution of net electronic gaming machine revenue from racetrack gaming facilities located in the southeast gaming zone that operates parimutuel greyhound racing by increasing the amount of revenue distributed to racetrack gaming facility managers from 25.0 percent to 67.5 percent. To balance out this increase, a corresponding reduction in revenues is in the bill. The state's share in the ELARF would be reduced from 40.0 to 22.0 percent; the share going to the Problem Gambling and Addictions Grant Fund would be reduced from 2.0 percent to 0.5 percent; the 1.0 percent share going to the Kansas Horse Fair Racing Benefit Fund would be eliminated; the 7.0 percent going to the Live Horse Racing Purse Supplement Fund would be eliminated; and the 15.0 percent share of gaming revenues would be eliminated. The share going to the Live Greyhound Racing Purse Supplement would remain unchanged at 7.0 percent and the share going to cities and counties would remain unchanged at 3.0 percent.

The bill would also remove the earning caps on both the Live Horse Racing Purse Supplement Fund and the Live Greyhound Racing Purse Supplement Fund. Under current law, the amount of electronic gaming machine revenue that is to be transferred to each of these funds is limited to an average of \$3,750 per machine per location.

The bill would require the official breed registering agencies for horses and greyhounds that have each been approved by the Racing and Gaming Commission, to make recommendations to the Commission on or before December 1, for the implementation of programs which would maximize the economic development benefits in rural Kansas. The bill would reduce the application fee from \$500 to \$50 for any fair association, horseman's nonprofit organization, or the national greyhound association of Abilene, Kansas. The organization licensing fee would be reduced from \$100 to \$25 for each day of racing. The bill would eliminate some of the restrictions on simulcasting and would allow county fair associations to operate simulcasting for additional days. The bill eliminates the requirement that a parimutuel licensee be a non-profit organization. The parimutuel racetracks would no longer be required to distribute net earnings from horse and greyhound races to qualifying nonprofits. The bill removes the Kansas residency requirement for all officers, directors, or members of an organization licensee that conducts parimutuel racing.

Before any casino manager, racetrack gaming facility manager, or facility owner licensee pays any prize that requires the completion of an Internal Revenue Service form W-2G, the

manager or licensee would be required to check if the winner is listed on the state debtor files maintained by the Department of Administration. If it is determined that the person is a state debtor, then the prize must be withheld to the extent of the amount owed. The manager or licensee would not be subject to any civil, criminal, or administrative liabilities for any prize that was mistakenly withheld provided that it was not due to any intentional, malicious, or wanton act by the manager or licensee. The only remedy for a person whose winnings are wrongfully withheld would be to submit an appeal to the Department of Administration. Withheld winnings must be submitted to the State Treasurer and credited to the Department of Administration's Setoff Clearing Fund. The Department of Administration would be permitted to work with the manager or licensee for the purposes of the state debt setoff program. The bill would clarify that this program would not apply to Native American Tribal gaming facilities.

The bill defines similar gaming facility as the portion of a building that is used for the purposes of operating, managing, and maintaining lottery facility games and other games authorized to be conducted or operated at tribal gaming facilities. Similar gaming facility does not include any facility authorized to operate, manage, and maintain only electronic gaming machines.

HB 2545 would not require additional staffing or expenditures by the Kansas Racing and Gaming Commission, the Kansas Lottery, or any other state agency unless a contract with a racetrack gaming facility manager is approved by the Kansas Lottery and a background investigation is approved by the Kansas Racing and Gaming Commission. Racetracks would first be required to obtain a parimutuel license from the Kansas Racing and Gaming Commission before they could negotiate with the Kansas Lottery for a contract to operate electronic gaming machines. The proposed changes to the distribution of gaming facility revenue could provide an incentive for the Woodlands Racetrack in Kansas City, Wichita Greyhound Park, and Camptown Greyhound Park in Frontenac to negotiate a contract with the Kansas Lottery in order to reopen these facilities with electronic gaming machines. A contract could not be approved with the Wichita Greyhound Park unless the voters of Sedgwick County first approve the operation of electronic gaming machines in a special election. The expenses of conducting a special election would be the responsibility of Sedgwick County. The Sedgwick County Election Commissioner has previously indicated that the costs associated with conducting a special election would be approximately \$124,000. However, the actual costs to conduct a special election may be higher.

The Kansas Lottery indicates that the state is prohibited from designating additional areas of the state where gaming facilities are authorized until July 1, 2032. Conducting a revote to allow Wichita Greyhound Park to reopen with electronic gaming machines may be viewed as an expansion of gaming that is prohibited under the Kansas Expanded Lottery Act. If it is determined that HB 2545 violates this provision, the state would be required to refund privilege fees from already selected casino managers plus a compounded annual interest rate of 10.0 percent that would total approximately \$122.0 million. Currently, the state has received \$61.0 million in privilege fees from four gaming facility managers and it is estimated that interest payments would be at least \$61.0 million. The accrued interest might be higher, if the judgement includes additional interest for litigation that is prolonged. The bill provides a mechanism for a racetrack gaming facility manager to pay or provide a line of credit for the payment of those fees and interest. In the event the casino managers are repaid privilege fees and interest, the line of credit amount would be used to repay the privilege fees and accrued interest; however, the racetrack gaming facility manager would be reimbursed for the payment amount to casino managers out of the state's share of revenue from the racetrack gaming facility that would be distributed to the Expanded Lottery

Act Revenues Fund. Furthermore, the redistribution of revenues, removal of the bidding process on 600 electronic gaming machines and perhaps other provisions of this bill, including post-contract amendments to terms of the law may also trigger breach of contract and related claims by the existing casino managers, which would be in addition to the claims for refund of privilege fees and interest.

The Attorney General's Office indicates the bill has the potential to significantly increase litigation costs starting in FY 2019. However, the Office did not provide an estimate of the additional litigation costs or how long the estimated litigation costs would continue from enactment from the bill, or if the bill would require the hiring of outside counsel.

The Kansas Lottery indicates that it would need to hire between two and three new employees for each new gaming facility that would open as a result of this bill. However, without knowing the size of the proposed facility and when the facility would open, the Kansas Lottery is unable to make an estimate of its gaming related expenses. The Kansas Lottery indicates that when it has negotiated contracts with gaming facility managers, it has required that all of its gaming related expenses be reimbursed by the manager. Direct gaming expenses are billed directly to the specific gaming facility manager and indirect expenses are prorated to all managers.

The Kansas Racing and Gaming Commission indicates it would need approximately \$1.8 million and 21.00 FTE positions for each parimutuel racetrack that reopens for the annual costs to regulate both the racing and gaming activities. Start-up costs of approximately \$450,000 per facility would also be needed for expenses, such as background investigations, licensing equipment, software licenses, computer equipment, furniture and supplies, and other expenses that would be associated with reopening each facility. Funding for regulating racing activities has primarily come from the transfer of parimutuel tax receipts to the State Racing Fund. The appropriations bill each year provides the authority for the Kansas Racing and Gaming Commission to bill each facility for all costs related to regulating racing activity. The requirements of the debt-setoff program would require additional staff time to modify regulations, facility operator internal controls, and audit programs. However, it is estimated that the costs associated with these activities would be negligible and, under the Kansas Expanded Lottery Act, would be reimbursed by gaming facility operators.

The Department for Aging and Disability Services indicates that additional gaming facilities would likely increase demand for services provided by its Problem Gambling Program. The Department indicates that the amount of additional spending would be dependent on the number of additional gaming facilities and would be proportional to current spending levels for problem gambling and addiction services. The Department also has concerns that additional gaming facilities and changes to the share of gaming facility revenues that is distributed to the Problem Gambling and Addictions Grant Fund would not provide adequate funding to support its Problem Gambling Program.

The Department of Administration indicates that expanding the debt setoff program would require computer programming to make sure that prizes or winnings at state-owned gaming facilities would be subject to the debt setoff program. The debt setoff program intercepts debts owed to state agencies, municipalities, district courts, and state agencies in other states. Debts include, but are not limited to child support, taxes, educational expenses, fines, services provided to the debtor, and court ordered restitution. The Department of Administration indicates that the

The Honorable John Barker, Chairperson

February 12, 2018

Page 6—HB 2545

costs associated with programming existing software to implement the debt-setoff requirements of the bill would be negligible and could be absorbed within existing resources. The Department of Administration indicates the bill would increase debt setoff revenue annually by up to \$100,000 starting in FY 2019 by requiring casino managers, racetrack gaming facility managers, or facility owner licensee to assist in the collection of debts. With an increase of \$100,000 in debt setoff revenue in FY 2019, the bill would also allow the Department of Administration to receive up to \$17,000 in collection assistance fees that would be used to help run the debt setoff program.

A reliable estimate of the gaming facility revenue that might be generated as a result of HB 2545 cannot be made without a detailed market study, which would include an estimate as to when the gaming facility would be operational, the location of the gaming facility, the size of the gaming facility, and if the new gaming facility would impact revenues from existing gaming facilities. Any fiscal effect associated with HB 2545 is not reflected in *The FY 2019 Governor's Budget Report*.

Sincerely,



Larry L. Campbell
Chief Budget Officer

cc: Stephen Durrell, Lottery
Brandi White, Racing and Gaming
Colleen Becker, Administration
Cody Gwaltney, Aging and Disability Services
Jackie Aubert, Children and Families
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