

State of Delaware

Video Lottery Advisory Council

November 5, 2015

Tom Cook
Secretary of Finance
State of Delaware
Carvel State Office Building
820 N. French Street
8th Floor
Wilmington, DE 19801

Dear Secretary Cook,

In accordance with Title 29, Chapter 29, Paragraph 4824 of the Delaware Code, attached is the 2015 Report of the Video Lottery Advisory Council (VLAC). This report contains legislative recommendations of the VLAC necessary to allow the Delaware gaming industry to be a viable resource for the State of Delaware, given the increasing competition and financial challenges facing the Delaware casinos. Members of the VLAC representing the Delaware Lottery and Scientific Games abstained from voting on the legislative recommendations included in the attached report.

Members of the Video Lottery Advisory are appreciative of the action that has been taken in the past as a result of recommendations made via the annual Report. I, as well as the other Delaware video lottery agent representatives who serve on the VLAC, look forward to discussing the recommendations in the attached report.

Sincerely,



Edward J. Sutor
Chairman
Attachment

State of Delaware

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2015 Report

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**Video Lottery Advisory Council
2015 Report**

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What is the competitive outlook for Delaware gaming?

The Delaware casino industry continues to be negatively impacted by increased regional competition. Since Pennsylvania started slot operations in 2007, Delaware has suffered through 34 calendar quarters of year over year declines in slot revenues, experiencing its first, slight quarter over quarter increase in the 3rd quarter of 2015. Delaware's table game revenues declined every quarter since Maryland began table game operations in 2013 until recently. The Delaware casino industry experienced its first quarter over increase in table game revenue in the 3rd quarter of 2015 only because the quarter to quarter comparison is now past the one year anniversary of the opening of Horseshoe Baltimore. The downward trend should be expected to continue, as the multi-billion dollar MGM Casino near Washington D.C. is under construction with a grand opening set for the second half of 2016 and Pennsylvania recently approved second casino in Philadelphia.

The Delaware casinos are appreciative for the financial relief extended by the legislature and the administration over the past several years; however, a long term solution is needed to address the financial difficulties the casinos are now experiencing.

What are the 2015 recommendations of the VLAC?

Due to the current state of the Delaware gaming industry and the intensifying competitive landscape, the following recommendations include major structural changes to the current revenue sharing and license fee model. All of the following recommendations were included in the 2014 VLAC Report to the State.

Legislative Recommendations

- **Recommendation #1: Modify the slot revenue share model - Reinstate the original tiered slot gaming tax structure established in 1994.**
 - *Justification: When slot operations began in Delaware, this was the way the revenue share structure was set up. As revenues increased, the State's share percentage increased; and conversely, if revenues decreased, the State's share percentage would also decrease. The switch to a fixed rate of 43.5% (after 6 prior increases) at a time when the competitive environment in the region was gaining momentum has created an unsustainable revenue share model that leaves the casino operators unprofitable and without the needed resources to properly staff, to market, and to reinvest in their facilities.*

- **Recommendation #2: Slot vendor fees, in their entirety, should be subtracted from slot revenues before being split among the parties in the slot revenue sharing model.**
 - *Justification: Sharing of Sports Betting and iGaming fees comes "off the top" and is therefore shared in its entirety by the State, Horsemen, and Video Lottery Agents. Currently, the State shares in 75% of slot vendor fees. It is recommended that, in the same form as Sports Betting and iGaming, 100% of the slot vendor fees be shared by the State, Horsemen, and Video Lottery Agents.*

- **Recommendation #3: Modify the table game revenue share model to be competitive with neighboring states – Adjust the table game revenue sharing rate to 15% and remove the annual license fee.**

 - *Justification: Delaware has the highest table game tax rate in the country. Maryland's rate is 20%, Pennsylvania's rate is 14%, and New Jersey's is 8%. With fees, Delaware's effective revenue share rate on table games is almost 40%, and combined with the overhead required in terms of payroll costs makes table games operations unprofitable for the State's 3 casinos. The Lottery and Gaming Study Commission included this recommendation in its report to the Administration and was included in, then removed from, Senate Bill 220 in 2014. It was also included in Senate Bill 30, introduced to legislature in 2015, which failed to reach the Senate floor for consideration.*

- **Alternative to Recommendation #3: Table game operations are extremely labor intensive. Allow the labor costs of table game operations to be subtracted before table game revenues are shared among the parties within the table game revenue sharing model and remove the annual license fee.**

 - *Justification: Slot machines are leased to the State by slot vendors who collect a lease fee. Table games are run by dealers who are employed by the casino at personnel costs upwards of 50% of table game revenues. It is recommended that, just as the State is sharing in slot machine vendor fees, the State allow the casinos to recover table game personnel costs prior to revenue sharing splits. The goal of implementing table game operations in Delaware was to increase gaming revenue and to create jobs. Table game operations, under this revenue share model, have consistently been unprofitable for the casinos since inception.*

- **Recommendation #4: Implement a revenue share credit of 5% to the casinos to encourage capital expenditures and 5% to encourage marketing initiatives.**

 - *Justification: This recommendation was also included in the preliminary Lottery and Gaming Study Commissions report to the Administration in 2013, but was removed from the final report prior to submission to the legislature. It was also included in Senate Bill 30 in 2015. Many of the gaming states in this region offer similar incentives; West Virginia gives a capital expenditure incentive to its casinos and offers a subsidy for advertising, New Jersey recently assisted Harrah's Atlantic City in their \$140 million convention center project. New York offers its casinos an advertising subsidy up to 8% of revenue. These types of incentives are used widely in the industry as a way for the state and the casinos to partner for the greater good of all parties.*

What is the VLAC?

The Video Lottery Advisory Council (VLAC) (aka the Advisory Council on Video Lottery Planning) was formed under House Bill #269 on June 19, 2003 to serve in a planning and advisory capacity to the Secretary of Finance.

What is the purpose of the VLAC?

Per Title 29, Chapter 48 of the Delaware Code:

The purpose of the VLAC is to consider matters relating to the growth and competitive vitality of the video lottery industry in the State, including but not limited to the following:

- (1) The status of video lottery game development issues in the State;
- (2) The status of known game problem resolution;
- (3) Personnel issues and concerns affecting the industry;
- (4) The effectiveness of current operational procedures and recommendations for new operational procedures or regulations;
- (5) The competitive vitality of the video lottery industry in the state, and recommendations for marketing and technological improvements;
- (6) Issues and concerns relating to the repair and maintenance of video lottery machines and related equipment, including preventive maintenance programs;
- (7) Video lottery agent or manufacturer specific projects that will impact the operation of the video lottery; and
- (8) Issues and concerns of the State Lottery Office relating to the video lottery operations and the status of internal control approvals.

The VLAC shall submit a report on its activities to the Secretary of Finance by November 5 of each year, together with recommendations for legislative and/or administrative changes it deems desirable. (Emphasis added.)

What is the Mission Statement of the VLAC?

“To provide a forum for video lottery officials, agents, and vendors to routinely address and resolve issues related to maintaining and improving the utmost in program integrity and operational efficiency. The VLAC shall render an annual report to the State on the results of its efforts and include recommendations to improve the program’s viability and to maximize the program’s growth in an increasingly competitive regional market.”

Who serves on the VLAC?

Per Title 29, Chapter 48 of the Delaware Code:

Membership on the VLAC shall include:

- (1) The Director of the State Lottery Office. (Vernon Kirk 302-744-1600)
- (2) One member from each licensed video lottery agent, to be designated by the respective agent. (Edward J. Sutor – Dover Downs Hotel & Casino 302-857-3206, Patti Key – Harrington Raceway 302-398-5913, Bill Fasy – Delaware Park 302-994-2521 ext. 2201)
- (3) Two members representing all of the licensed manufacturers of the video lottery machines to be designated by the Director of the State Lottery Office, and/or the licensed manufacturer of the central computer systems to be designated by the Director of the State Lottery Office. (Kathy Wayne – Scientific Games 302-678-7730, Michael Ordille – IGT 609-484-6424, Michael Nickolich – Bally 702-532-8484)

The Governor shall designate one member to serve as Chairperson of the Council, who shall serve in that capacity for two years and shall be eligible for reappointment. (Edward J. Sutor – President & CEO for Dover Downs Hotel & Casino – Term 2006 - 2007, reappointed 2008 – 2009, 2010-2011, 2012-2013, 2014 - 2015).

How often does the VLAC meet?

Per Title 29, Chapter 48 of the Delaware Code:

The VLAC usually meets quarterly, and a meeting can be called by the Director, the Chairperson, or a majority of the members.

When & where did the VLAC meet in 2015?

VLAC meetings during 2015 were as follows:

<u>Date</u>	<u>Time</u>	<u>Place</u>
April 28, 2015	1:00 p.m.	Dover Downs Hotel & Casino
July 28, 2015	1:00 p.m.	Dover Downs Hotel & Casino
September 22, 2015	1:00 p.m.	Dover Downs Hotel & Casino
October 27, 2015	1:00 p.m.	Dover Downs Hotel & Casino

All of the VLAC meetings were open public meetings. Minutes of the VLAC meetings are available on the State of Delaware website.