

State of Delaware

Video Lottery Advisory Council

November 5, 2013

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 2013 Report of the Video Lottery Advisory Council (VLAC). This report contains legislative and administrative recommendations of the VLAC necessary to allow the Delaware gaming industry to remain competitive, given the increasing changes to the mid-Atlantic gaming environment. Members of the VLAC representing state office or the slot machine industry abstained from voting on the legislative recommendations included in the attached 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

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What is the competitive outlook for Delaware gaming?

Delaware slot revenues have declined since the opening of the first Pennsylvania casino, Harrah's Chester, in January of 2007, and Delaware casino operators continue to struggle amid the influx of new casino options offered to residents in the Mid-Atlantic region. In addition to Pennsylvania and Maryland's maturing casino businesses, several major casino industry operators (Caesar's and MGM) are planning and building luxury casino resorts in Prince George's County and Baltimore. Steve Wynn is working to secure the second casino operating license in Philadelphia. Our regional landscape has and continues to drastically change, and referencing the Lottery's 2012 Annual report – Change Brings Opportunity. The Video Lottery Advisory Council recognizes an opportunity shared between the State of Delaware and the Delaware Video Lottery Agents to modify the revenue share models that were put in place during a significantly different competitive era to reflect Delaware's current competitive environment. In turn, this adjustment to the revenue share model would allow Delaware casinos to continue to contribute to the State's General Fund, as well as continue to employ thousands of Delawareans.

What are the 2013 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. *It is noted that members of the VLAC representing state office or the slot machine vendors, in respect of the sensitivity of their position, abstained from voting on the inclusion of the following recommendations.*

Legislative Recommendations

- Modify the slot revenue share model - Reinstate a tiered slot gaming tax structure and take vendor costs off the top.
 - *Justification: Given that the Delaware gaming industry has been faced with steadily declining slot revenues, with additional competitive pressure and no real sign of economic improvement in the near future, a high fixed rate model is no longer workable. A tiered structure, similar to the structure in place when slots began in Delaware, is necessary to allow the state to retain its larger share when business is strong, but also to lessen the burden on the video lottery agents during downturns.*
 - *Currently, vendor costs are taken from casino revenues after the State's share. Therefore, any increase in vendor costs are absorbed from the video lottery agent's share. If vendor costs are taken "off the top", then any increase in cost is shared among the State, the horsemen, and the video lottery agents.*
- Modify the table game revenue share model to be competitive with neighboring states
 - Adjust tax rate, remove the license fee, and take table game vendor costs off the top
 - *Justification: New Jersey's table game tax percentage is 8%. Although seemingly low, this is a lucrative rate for the state because table revenue*

makes up 30% of New Jersey's total gaming revenue. Maryland opened table game operations at three of their four casinos in April 2013 at a 20% tax rate. Pennsylvania's table game tax rate was decreased to 14% after 2 years of operations to make sure Pennsylvania table game operators were in a position to compete with the increase in table game options in the region. Pennsylvania's table game revenue contributes 25% of the state's total gaming revenue. Delaware's table game tax is 33.9%; Delaware table game revenues make up approximately 10% of casino revenues. Given the high table game tax rate, Delaware casinos do not have the ability to market at the same level as our neighboring, regional competitors. Delaware table game revenue is being entirely consumed by gaming taxes, license fees, and payroll and operating expenses. Relief in the form of reducing the table game tax rate to 14% (same as PA, yet still higher than AC), would allow Delaware video lottery agents to retain the 1,500+ jobs created by table game operations and extend better offers to our customers, increasing our competitive vitality and positively impacting casino revenue and the state's share.

- Modify the iGaming revenue share model – remove the \$3.75 million threshold and reduce the iGaming tax rate to 15% (same as New Jersey)
 - *Justification: Delaware's internet gaming revenue sharing rates in the current law are identical to that of the existing video lottery revenue sharing model. The State's current internet gaming revenue sharing rates are, therefore, unworkable using generally accepted internet gaming models. The two other states with approved iGaming are Nevada and New Jersey. Nevada went live with a 10% iGaming tax rate; New Jersey will go live with a 15% tax rate in November 2013. Delaware's iGaming slot tax rate is approximately 54%.*
 - *All three Delaware video lottery agents have been working closely with the State and the State-selected vendors to ensure a successful rollout and to be the nation's first, legal internet gaming state. With the project rolling out during the 4th quarter of 2013, approximately 8 months of iGaming revenue will be included in the current fiscal year. With the revenue model set up for the first \$3.75 million of iGaming revenue to go directly to the State, there will be very little, if any, iGaming revenue for video lottery agents during this kick-off year.*

Administrative Recommendations

- Improve casino directional signage on major roadways
 - *Justification: Delaware's neighboring casino industry competitors, Maryland and Pennsylvania, have major interstate exit and highway signage directing visitors to their casino locations. With the many changes and improvements recently made to Delaware's highways and interstates in New Castle County, there is an opportunity for the State to improve directional signage on these heavily traveled corridors, especially in Northern Delaware.*

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. **(Brennen Lawrence – Scientific Games 770-664-3827, Tim Shortall – IGT 609-484-6301, Robert Neugebauer – Spielo 302-376-1100)**

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, and 2012-2013).**

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 2013?

VLAC meetings during 2013 were as follows:

<u>Date</u>	<u>Time</u>	<u>Place</u>
April 2, 2013	1:00 p.m.	Dover Downs Hotel & Casino
July 9, 2013	1:00 p.m.	Dover Downs Hotel & Casino
September 10, 2013	1:00 p.m.	Dover Downs Hotel & Casino
October 29, 2013	1:00 p.m.	Dover Downs Hotel & Casino

All of the VLAC meetings were open public meetings and advanced public notice of each meeting was provided. Minutes of the VLAC meetings are available on the State of Delaware website.