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BILL



ANALYSIS

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Senate Bills 203, 204, and 205 (as reported without amendment)

Sponsor: Senator Mike Kowall (S.B. 203 & 204)

Senator Joe Hune (S.B. 205)

Committee: Regulatory Reform

## **CONTENT**

Senate Bill 203 would create the "Lawful Internet Gaming Act" to do the following:

- Allow internet gaming to the extent that it was carried out in accordance with the proposed Act.
- Create the Division of Internet Gaming in the Michigan Gaming Control Board, and prescribe its responsibilities.
- Allow the Division to issue applicants an internet gaming license if they met certain criteria.
- Prescribe a \$100,000 application fee, a \$200,000 initial license fee, and a \$100,000 annual fee for an internet gaming license.
- Allow an internet gaming license to be issued only to a casino licensee or, under certain conditions, to a Michigan Indian tribe that operates a casino in the State.
- Allow the Division to license internet gaming vendors to provide goods, software, or services to internet gaming licensees.
- Prescribe a maximum \$5,000 application fee, a \$5,000 initial license fee, and a \$2,500 annual fee for an internet gaming vendor.
- Require an internet gaming platform provider to pay an initial license fee of \$100,000, and \$50,000 each year after the initial license was issued.
- Provide that a license would be valid for five years and could be renewed for additional five-year periods.
- Impose a tax of 10% on the gross gaming revenue received by an internet gaming licensee from internet gaming, but provide for the tax rate to be reduced to a rate equivalent to that provided in a compact, amendment to a compact, or other agreement negotiated with the State.
- Require an internet gaming licensee to have adequate gaming participant verification measures, including mechanisms to detect and prevent the unauthorized use of internet wagering accounts and to detect and prevent fraud, money laundering, and collusion.
- Allow the Division to develop responsible gaming measures, including a statewide responsible gaming database identifying individuals who were prohibited from establishing an internet wagering account or participating in internet gaming.
- Allow the Division to enter into agreements with other jurisdictions to facilitate, administer, and regulate multijurisdictional internet gaming to the extent that entering into an agreement was consistent with State and Federal laws and if the gaming under the agreement were conducted only in the United States.
- Create the "Internet Gaming Fund" and require fees and taxes to be deposited into the Fund.
- Allow the Michigan Gaming Control Board to spend money from the Fund, on appropriation, for the First Responder Presumed Coverage Fund (which could receive \$5.0 million annually) and the Board's costs of regulating and enforcing internet gaming.
- Prescribe a felony penalty of imprisonment for up to 10 years and/or a maximum fine of \$100,000, for a person who committed an action prohibited by the Act.

Senate Bill 204 would amend the Michigan Penal Code to exclude gaming conducted under the proposed Lawful Internet Gaming Act from Chapter XLIV of the Code, which prescribes penalties for illegal gambling activities.

Senate Bill 205 would amend the Code of Criminal Procedure to include the offense proposed by Senate Bill 203 in the sentencing guidelines as a Class D felony against public order.

Proposed MCL 750.310c (S.B. 204)  
MCL 777.14d (S.B. 205)

Legislative Analyst: Drew Krogulecki

### **FISCAL IMPACT**

Senate Bill 203 would have an indeterminate negative impact on the City of Detroit, result in additional expenses to the Michigan Gaming Control Board, generate additional revenue to the First Responder Presumed Coverage Fund, and have an indeterminate impact on the General Fund and School Aid Fund. There are a number of factors that would affect revenue in a variety of ways. Much of the variation in estimates arises from the extent to which Internet Gaming Fund revenue would supplant revenue from other gaming activities. No state that has introduced internet gaming while also having casinos and a state lottery has yet to have an overall increase from all three sources, so it is difficult to estimate an overall revenue increase with the introduction of internet gaming for the State of Michigan. However, it is possible that the State could experience an overall increase even if internet gaming revenue is taken from other gaming activities.

Furthermore, more felony arrests and convictions could increase resource demands on law enforcement, court systems, community supervision, jails, and correctional facilities. The average cost to State government for felony probation supervision is approximately \$3,024 per probationer per year. For any increase in prison intakes, in the short term, the marginal cost to State government would be approximately \$3,764 per prisoner per year. Any associated increase in fine revenue would increase funding to public libraries.

Lottery. It is likely that the Michigan Lottery's instant lottery and internet iLottery would directly compete with internet gaming in the State since these games are similar in that they are played day-to-day as opposed to the larger lottery games, which have more activity when jackpots are large and less activity when jackpots are smaller. Instant ticket games currently account for 36% of total Lottery revenue (up from 33% four years ago), and they accounted for 57% of the total increase in lottery revenue over the past four years (\$628.0 million). The iLottery, which totaled \$48.0 million in revenue in fiscal year 2015-16, the largest amount since its introduction in 2014, would be the most directly in competition with internet gaming. In the long term, the iLottery and instant ticket games could move to internet gaming. It is estimated that between 1% and 3% of Lottery revenue could move to internet gaming, but accounting for the amount of instant gaming activity, this amount could be up to 5% in the long term (beyond four years). The amount of State Lottery revenue that goes to the School Aid Fund (SAF) is roughly 28%, while internet gaming would be taxed at 10%. This means that for every 1% decrease in Lottery revenue (\$31.2 million in total revenue with \$8.6 going to the School Aid Fund), there would be a net loss to the State of \$5.5 million since internet gaming would raise only \$3.1 million for the Internet Gaming Fund. For the long term, if the State Lottery were to lose 3% to 5% of revenue to internet gaming, the State would lose between \$16.5 million and \$27.5 million in SAF dollars.

Another way to think about the revenue shift is that for every 1% decrease in total State Lottery activity due to internet gaming, the internet gaming would need to generate \$86.0 million in order to be revenue neutral; and for every 3% decrease in Lottery activity, the internet gaming revenue would need to be \$258.0 million. It is projected that internet gaming revenue would generate \$220 million to \$280 million over the long term, so it is possible that

internet gaming could be revenue neutral if the loss to State Lottery were less than 3% and internet gaming met its expectations. However, if the loss were greater than 3% or it took longer for internet gaming to be established, then the State would experience a net revenue loss in the tens of millions of dollars.

Casinos. Casinos are taxed at 19% of "net win" (gross receipts less winnings paid to wagerers), with 8.1% going to the School Aid Fund and 10.9% going to the City of Detroit. Since internet gaming would be taxed at 10%, for every 1% decrease in casino revenue for internet gaming, the State would actually experience an increase of \$150,000. This means that even if there were a significant change in revenue from casinos to internet gaming, the State would largely remain revenue neutral. However, with the potential for a reduced tax rate due to a lower rate under a compact, this amount could be less.

City of Detroit. The City of Detroit would experience a revenue decrease as a result of internet gaming. If the Detroit casino revenue were to decrease between 1% and 3% due to internet gaming in the long term, the City would experience a revenue loss of between \$1.5 million and \$4.5 million. Since internet gaming would not produce revenue for the City of Detroit, the City would not have any way to mitigate the revenue loss.

Tribal Casinos. The bill could affect money received from tribal gaming in the event that additional Indian tribes declined to make payments, similar to what occurred when tribes declined to pay the State due to the opening of the three Detroit casinos and the introduction of the Lottery's iLottery games. These payments significantly fund the Michigan Economic Development Corporation (MEDC) and the Jobs for Michigan Investment Fund, and in FY 2014-15 totaled \$43.9 million. This revenue, however, is not included in the State revenue totals and is only represented in the Michigan Strategic Fund (MSF)/MEDC financial report. The State would experience a direct impact from the loss of tribal revenue to the MSF/MEDC only because some employees who are funded with the corporate funding administer some of the State-appropriated programs. The corporate funds also provide additional funding to State programs as well as other economic development programs. If the MSF/MEDC lost all of the tribal revenue, the State could have less administration of economic development programs or need to provide additional revenue to supplement the MSF and administer those programs.

School Aid Fund. The School Aid Fund would experience a loss due to any shift in gaming revenue to internet gaming even if overall State revenue remained revenue neutral. If the State Lottery revenue shifted to internet gaming in the long term by 3% to 5% and casino revenue shifted by 1% to 3%, the School Aid Fund would experience a loss of between \$27.0 million and \$46.7 million or roughly \$18 to \$32 per pupil. This could significantly affect appropriations from the School Aid Fund.

Administration. The bill would result in additional expenses to the Michigan Gaming Control Board to regulate and issue licenses for internet gaming, and internet gaming vendors. The applications and license fees would make up the majority of the administrative revenue for the Board. Since the initial licenses would be valid for five years, it is difficult to predict whether the administrative revenue would be sufficient to support the regulatory costs. However, the Department of Treasury estimates that the fee amount would be sufficient to cover the administrative expenses of internet gaming. If the Board needed additional revenue for administration, there would be an even greater overall negative impact on the State.

First Responder Presumed Coverage Fund. The bill would result in \$5.0 million in annual appropriations to the First Responder Presumed Coverage Fund. Using the introduction of the iLottery games to predict initial revenue, it is estimated to take two full years from introduction for revenue to be sufficient to make this annual appropriation.

Senate Bill 204 would have no fiscal impact on State or local government.

Senate Bill 205 would have no fiscal impact on local government and an indeterminate fiscal impact on the State, in light of the Michigan Supreme Court's July 2015 opinion in *People v. Lockridge* (in which the Court struck down portions of the sentencing guidelines law). According to one interpretation of that decision, the sentencing guidelines are advisory for all cases. This means that the addition to the guidelines under the bill would not be compulsory for the sentencing judge. As penalties for felony convictions vary, the fiscal impact of any given felony conviction depends on judicial decisions.

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