

HOLLYWOOD
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AT KANSAS SPEEDWAY®

TESTIMONY

HB 2173

An Act concerning gaming; relating to the Kansas Expanded Lottery Act

House Appropriations Committee

March 23, 2017

Good morning Chairman Waymaster and Members of the House Appropriations Committee:

Kansas Entertainment, LLC appreciates the opportunity to present testimony to the Committee in opposition to HB 2173 and share with you what we see as the potential financial ramifications for the State of Kansas from passage of this legislation that you will not hear with clarity from the proponents.

By way of information, Kansas Entertainment, LLC is a joint-venture partnership of Penn Hollywood Kansas, Inc., and Kansas Speedway Development Corporation, and was selected by the State of Kansas in 2009 to develop a destination casino for the Northeast Kansas Gaming Zone.

The Kansas Legislature passed legislation in 2007 to allow for expanded gaming in our state after more than a decade of proposals from various developers and interested parties. We believe a review of history is important to your consideration of this issue, as there are not many legislators serving today who were here in 2007 – I believe only two members of this 23-member committee voted on SB 66 that allowed for the expansion of gaming in Kansas.

When the Kansas Legislature approved the expanded gaming bill – SB 66, the bill was written in a way to insure the State received the best possible proposals from casino developers by dividing the state into four gaming zones with one casino allowed in each zone with a minimum investment required and a competitive bidding process created in statute. At that time, there were three pari-mutuel tracks in Kansas and they were each granted authority to place slot machines in their facilities with a higher tax rate for their machines, as they did not have to compete for a license and had no minimum investment requirement.

In 2007, there were two pari-mutuel track operators in Kansas: Bill Grace owned The Woodlands in Wyandotte County and Phil Ruffin owned Wichita Greyhound Park and Camptown Greyhound Park in southeast Kansas. The track owners had significant input in drafting the legislation and strongly supported its passage. In fact, there was a ceremonial bill signing ceremony at The Woodlands with Governor Kathleen Sebelius, Mr. Grace and representatives of the pari-mutuel industry.

One of the requirements of SB 66 was that expanded gaming had to be approved by the voters in the county where gaming would take place. This requirement proved to be a fatal flaw in the plans for Mr. Ruffin and his proposal for slots at the Wichita Greyhound Park, as Mr. Ruffin missed the layup, so to speak, and the voters of Sedgwick County in a special election in 2007 voted to not allow gaming in their county.

After the vote in Sedgwick County prevented Mr. Ruffin from placing slots at Wichita Greyhound Park, he persuaded The Woodlands to not open their facility for gaming and instead let their lobbyists head back to the Statehouse in 2008 and negotiate a better deal, including a revote in Sedgwick County. We are now in the tenth year of a Ruffin-led effort to cut the state's share of gaming revenues for the benefit of the pari-mutuel track owners, which is now special interest legislation just for Mr. Ruffin, who owns all three mothballed major pari-mutuel tracks in Kansas.

Under SB 66, the state receives 25% of the slot revenue and an additional 15% for expenses, for a total of 40% of the slot revenues, one of the lowest blended tax rates for slot machines at racetracks in the country. Massachusetts and Pennsylvania, by comparison, tax slot machines at racetracks at 49% and 55%, respectively, and Penn National Gaming, a 50% owner of Hollywood Casino at Kansas Speedway, successfully operates facilities in each of those jurisdictions. Given the competitive cost of labor, lower transportation costs and availability of feed stock and veterinary services in our state, the owner's percentage in Kansas is extraordinarily fair and one that was agreed upon by the track owners.

A question we are asked is, "Why does the casino care what the tax rate is at the pari-mutuel tracks?" The answer lies in the well-thought logic behind SB 66 and the State's interest in soliciting the best, most competitive proposals for a destination casino in four market areas.

Casino developers engaged in a highly competitive process with multiple applicants in every gaming zone. Criteria used by the Lottery Gaming Facility Review Board to evaluate proposals included:

- Size of the proposed facility;
- Geographic area in which the facility is to be located;
- Facility's location as a tourist and entertainment destination;
- Estimated number of tourists that would be attracted to the proposed facility;
- Number and type of lottery facility games to be operated at the facility; and,
- Agreements related to ancillary lottery gaming facility operations.

Casino developers in the Northeast Kansas Gaming Zone were required to invest at least \$225 million and pay a \$25 million privilege fee. To win the license, Kansas Entertainment committed to invest more than \$300 million and create a true destination gaming facility.

A part of the Kansas Entertainment proposal also was to construct a hotel on the property or, after a certain period of time, remit to the Unified Government a payment in lieu of constructing the hotel. When first granted a license, market research did not support the construction of a hotel. Kansas Entertainment does not believe the market would yet support a hotel and began payment of 1% of gaming revenues to the Unified Government as required under its agreement with them. This amounts to approximately \$1.4 million per year. Kansas Entertainment remains committed to a hotel on its property as well as additional investments. However, until such a time as the regulatory climate has stabilized (e.g., consideration of expanded gaming legislation and its impact on Hollywood Casino at Kansas Speedway is resolved), the owners cannot commit to construction of a hotel on the property.

In addition, as part of their successful bid, Kansas Speedway agreed to solicit the governing body of NASCAR for a second Cup race for their facility. They were indeed granted a second race, which has become a highly-prized championship race later in the season. These races are each a \$120 million economic bonanza for our area, which is like having two Super Bowls in our state every year.

Hollywood Casino at Kansas Speedway Snapshot:

- More than \$300 million invested in casino facility;
- Approximately 700 employees;
- In-state purchasing: ~\$7 million annually;
- State Taxes Paid: ~\$38 million in 2016 (~\$179 million to date);
- Funds to Unified Government of WyCo: ~\$2.9 million in 2016 (~\$10.4 million to date);
- Property Taxes: ~\$7mm in 2016 (~\$33 mm to date);
- Charitable Contributions: ~\$1 million annually.

In summary, the greater percentage of revenue is allowed for the destination casino owner because they have to cover the costs of significantly higher investment, compared to no investment threshold for the pari-mutuel track owners.

What are the criteria in SB 66 for licensing a slots-at-track proposal? There are none. Track owners were guaranteed their license for a slot parlor merely for owning a pari-mutuel track with no requirements for investment in infrastructure, appeal to tourists of investment in ancillary operations. Giving the pari-mutuel facilities the same tax rate as the destination casinos fails to recognize the cost of the ancillary investments the casino managers were required to make to win their respective licenses.

To insure the State received the best possible proposals from its casino management applicants, SB 66 included language to prohibit a further expansion of gaming in Kansas. The contracts with the four licensed casinos also contain provisions that limit the state's ability to expand gaming further than that allowed under SB 66. Should the state violate these provisions, the remedy available to the casino operators is a return of their privilege fee with ten percent interest from the time the fee was paid. In the case of Hollywood Casino at Kansas Speedway, that date is September, 2009.

Setting aside for a moment the unfairness of the State subsidizing the operations of a track owner who by all information available doesn't need it, we wish to note specific objections to HB 2173 and make this Committee aware of the potential financial ramifications of this legislation.

HB 2173 is the most creative gaming bill we have seen to date regarding Mr. Ruffin's attempt to shield the State from potential liability for breach of contract actions by the owners of the four licensed destination casinos. However, we do not believe it would withstand judicial review. The drafters rather in artfully seek to force the state to breach its agreements with all four destination casinos.

One of the provisions of HB 2173 is language allowing for a revote in Sedgwick County of the question as to whether to allow for slot machines to be placed at Wichita Greyhound Park.

In 2016, Attorney General Derek Schmidt was asked to render an opinion on whether legislation allowing a second vote in Sedgwick County on the expanded gaming question that if successful would allow for the placement of slot machines at Wichita Greyhound Park would violate the state's contract with the South-Central Facility Management contract and Kansas statutes prohibiting such additional gaming location and trigger repayment of the privilege fee, compounded annually at the rate of 10%.

The answer in AG Opinion No. 2016-6 was Yes.

The following is a quote from page 10 of the 23-page opinion:

“Thus, the specific question we are answering as your first question is this: Would enactment of the provision of 2016 House Bill 2537 that authorizes a revote on the placement of EGMs at a racetrack facility in Sedgwick County render the State liable to refund the privilege fee paid to the State under terms of the lottery gaming facility management contract between the Kansas Lottery and the lottery gaming facility manager in the south central gaming zone?”

We think the answer to that question is yes for three separate reasons, any of which standing alone would lead to the same conclusion. First, a breach of contract likely would arise...”

Kansas Entertainment strongly encourages this Committee to review this opinion in its entirety before considering this legislation. We also believe the Kansas Attorney General should be requested to review this opinion for the Committee in conjunction with any consideration of expanding gaming in Kansas through legislation like HB 2173.

The proponents of this legislation attempt to dodge this issue and potential liability by creating a substantial financial barrier to litigation. Should this legislation pass, the four licensed casino owners would purportedly be required to proffer a \$5 million bond to litigate or intervene in any suit challenging the constitutionality or validity of the legislation – essentially a bet that the legislation is unconstitutional or prohibited under SB 66. Should the intervener be successful, they would receive back their \$5 million payment and be entitled to receive back their privilege fee compounded annually at the rate of 10%. Any casino manager who failed to remit the bond would be precluded from receiving a refund of their privilege fee and interest. Should legislation be upheld, the state would receive that money as liquidated damages for filing the suit, with the track owners repaid for their attorney fees and costs.

In HB 2173, Mr. Ruffin suggests he would provide a bond to cover any liability the State may incur for losing such suit. However, should the bond ever be forfeited for a breach under the bill, Ruffin gets repaid his money from the State’s share of gaming revenues.

K.S.A. 74-8734(h)(19) states:

“Any management contract approved by the commission under this section shall...(19) include enforceable provisions: (A) Prohibiting the state, until July 1, 2032 from (i) entering into management contracts for more than four lottery gaming facilities or similar facilities, one to be located in the northeast Kansas gaming zone, ...”

The proponents also seek to change the terms of judicial review for a violation, as they preclude the court in the bill from considering whether placement of slots at a pari-mutuel track would be deemed to be a “similar gaming facility.” This is another violation of an existing contract between the State of Kansas and the lottery gaming facility managers.

These provisions would clearly violate contracts with the four lottery gaming facility managers, which were set in place and agreed upon based upon the language of SB 66, not SB 66 as it might subsequently be amended. As such, changing the terms of what constitutes a breach of contract cannot be imposed upon the lottery gaming facility managers by subsequent standards of review, imposition of financial liability for exercising contractual rights or seeking redress in the courts.

Kansas Entertainment suggests this Committee ask the Kansas Lottery to review the four Lottery Gaming Facility Management contracts entered between the State of Kansas and the respective casino operators before considering this legislation as well.

When legislation proposed by Mr. Ruffin was considered in 2016, the potential liability for violating the lottery gaming facility manager contracts and triggering repayment of privilege fees and interest was estimated at approximately \$100 million dollars. That number is higher today, given the additional interest that has accrued since that time. The fiscal note on HB 2173 indicates this liability is approximately \$112 million, should it be incurred. And, this number is only for the privilege fee and accrued interest. The State could very well be liable for additional damages, including future lost profits under a breach of contract action.

Kansas Entertainment does not believe the terms required to challenge this legislation will withstand legal review. The cause of action that lies with violation of K.S.A. 2016 Supp.74-8734(h)(19) or K.S.A. 74-8741(c)(4) or any other provision of SB 66 not only lies within statute, but also within the contract Kansas Entertainment has with the State of Kansas. Accordingly, Kansas Entertainment will not find itself limited by Mr. Ruffin's attempts to rig the verdict, but rather the State of Kansas will be the entity subject to a breach of contract action with all the risk of financial loss clearly at its feet, not those of Mr. Ruffin.

These efforts have been going on now for ten years. It is time for the State of Kansas to say enough is enough and tell Mr. Ruffin to live up to the promises he made to the breed groups in Kansas ten years ago. Open your tracks and bring pari-mutuel racing back to Kansas under the terms he negotiated and agreed to in SB 66.

Mr. Ruffin clearly has the financial resources and legal ability to open at least one of his facilities – Wyandotte County or Crawford County and allow for the racing of horses and greyhounds. Nothing in state law prevents him from doing so.

Should he ever actually open one of his tracks, we would respectfully suggest the State would then be in a much better position to evaluate whether pari-mutuel racing can be profitable under the terms agreed upon by all parties concerned in 2007, or whether the efforts of Mr. Ruffin to renegotiate a deal he made ten years ago is nothing more than a veiled attempt to obtain a financial windfall at the expense of the State of Kansas and its partners, the casino owners, who have more than lived up to the promises they have made and will continue to do so in the years to come.

Kansas can't afford HB 2173 and we respectfully request the committee not pass this legislation to the floor.

Thank you for the opportunity to present our concerns to the Committee today.

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