NORTH CAROLINA GENERAL ASSEMBLY

2021 Session

Legislative Fiscal Note

Short Title: Sports Wagering Amendments.
Bill Number: Senate Bill 38 (Third Edition)
Sponsor(s): Rep. Johnson, Sen. Jim Perry, Sen. Michael A. Lazzara, and Sen. Todd Johnson

SUMMARY TABLE

FISCAL IMPACT OF S.B. 38, V.3 ($ in millions)

	FY 2022-23	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27
State Impact					
General Fund Revenues	10.66	13.41	12.36	15.56	16.97
Less Expenditures	4.68	4.96	5.57	6.06	6.28
General Fund Impact	**5.98**	**8.45**	**6.79**	**9.50**	**10.69**
Special Fund Revenues	0.51	1.69	3.40	4.76	5.34
Less Expenditures	-	-	-	-	-
Special Fund Impact	**0.51**	**1.69**	**3.40**	**4.76**	**5.34**
NET STATE IMPACT	**$6.49**	**$10.14**	**$10.19**	**$14.26**	**$16.03**
STATE POSITIONS	**8.00**	**8.00**	**8.00**	**8.00**	**8.00**

FISCAL IMPACT SUMMARY

The bill modifies several finance-related components of SB 688 (v4). The bill changes the taxing structure from the State receiving 8% of Adjusted Gross Wagering Revenue (AGWR)[1] to a privilege tax of 14% on AGWR[2] and makes several changes to the calculation of the tax. Further, it adds parimutuel betting to the types of gambling allowed.[3] In addition, the bill raises the fees associated with applying for and maintaining various licenses. The bill also changes the date sports betting could begin to January 1, 2023. After applying various revenue-generating and -reducing factors authorized in the bill, Fiscal Research estimates total tax and fee revenue of $11.2 million in FY 2022-2023 and increasing to $22.3 million in Fiscal Year 2026-2027. Licensure fees assessed by the Lottery Commission are estimated to generate approximately $6.5 million in both Fiscal Year

[1] In Version 4 of SB688, AGWR was essentially the net of all sports wagers received minus winnings, promotional credits, and other reductions to revenues.
[2] AGWR differs from Gross Gaming Revenue (GGR) in that GGR is defined by the Spectrum reports as "the amount retained after all winning wagers have been paid, but before any expenses or taxes have been deducted."
[3] Parimutuel betting involves betting against other betters on the same event, rather than against the "house."

2022-23 and FY 2023-24. Any fee revenue that is not used to cover the Lottery Commission's administrative expenses will be remitted to the General Fund. Of the amount of tax revenue, each year the Department of Revenue retains $0.5 million to off-set the cost of collection, $2.0 million is dedicated to the Department of Health and Human Services gambling addiction education and treatment programs, and $500,000 is dedicated to the North Carolina Parks and Recreation Authority for $5,000 grants to each county for youth sports development.[4] Of the remaining amount:

- 10% is to be distributed equally to the following UNC-constituent institutions to support collegiate athletic departments: Elizabeth City State University, Fayetteville State University, North Carolina Agricultural and Technical State University, North Carolina Central University, the University of North Carolina at Asheville, the University of North Carolina at Pembroke, and Winston-Salem State University;
- 30% to the North Carolina Major Events, Games, and Attractions Fund; and
- 60% to the General Fund.

FISCAL ANALYSIS

Revenue Generating Provisions

Session Law 2019-217 (SB 574) directed the North Carolina Lottery Commission to study gambling in general in the state and asked the Commission to "provide an independent analysis of current North Carolina gaming activities (including those prohibited by law), potential new gaming activities and whether a Gaming Commission should be created in North Carolina." That law directed the Lottery Commission to study the following relating to sports betting:

- Any authorizations and restrictions on such activities in this State;
- Any effects of authorizing sports betting on existing tribal games in this State and on lottery activities, if any;
- The positive and negative impacts of authorizing sports betting in this State;
- Potential revenues and expenditures for the State, if sports betting is authorized; and
- Appropriate regulation and oversight of sports betting, including potential licensing of operators.

The Lottery Commission contracted with Spectrum Gaming Group (Spectrum) to complete both studies.[5] Spectrum issued its report on sports betting in December 2019,[6] followed by the more

[4] The bill states that if there are not sufficient funds for the $500,000 annual appropriation to the North Carolina Parks and Recreation Authority, the amount of each grant counties receive shall be reduced by the same proportion so that all counties receive a grant of the same amount.

[5] Per its website and the reports submitted to the North Carolina Education Lottery, Spectrum Gaming Group is a non-partisan consultancy that specializes in the economics, regulation and policy of legalized gambling worldwide. It further states they have provided independent research and professional services to public- and private-sector clients since 1993, brings wide industry perspective to every engagement, having worked in 41 US states and territories and in 48 countries on six continents. The sports betting report referenced below states that Spectrum has more than 250 clients including government entities of all types and gaming companies (national and international) of all sizes, both public and private.

[6] Spectrum Gaming Group (2019). *Gaming Market Analysis: Analysis and Business Case of Impact of Regulating and Operating Sports Betting Through the North Carolina Education Lottery.*

general study of gambling in the state in March 2020.[7] Because the General Assembly commissioned the studies, and they were conducted by a firm with demonstrated experience and expertise in the field, Fiscal Research relied primarily on these reports as the basis to arrive at estimates for the revenue-generating portions of the bill. For brevity of text and simplicity, Fiscal Research refers to these two reports as the "Spectrum report(s)" throughout this memo.

The bill replaces S.B. 688's 8% tax on Adjusted Gross Wagering Revenue (AGWR) with a 14% privilege tax on AGWR. The tax would be calculated against gross wagering revenue (GWR) minus the following to arrive at AGWR:

- Winnings paid to registered players;
- Costs paid for any personal property distributed to a registered player as a result of a sports wager;
- Promotional credits or bonuses given to registered players, at cash value, when returned to the operator in the form of a wager or deposit, which would be phased out beginning in 2025;
- Uncollectible receivables from registered players, not to exceed 4% of gross wagering revenue; and
- Federal excise tax payments.

To estimate the amount of tax revenue that would be generated, Fiscal Research relied largely on the Spectrum report's projected Gross Gaming Revenue (GGR) derived from digital devices.[8] Fiscal Research made an adjustment increasing GGR because the bill authorizes certain bars and restaurants to accept sports bets, specifically based on location and affiliation. The Spectrum report's estimated impact of bars and restaurants offering sports betting onsite included these establishments to a much broader degree when compared to those authorized by the bill, but not in the digital sports betting estimate. To make an adjustment for bars and restaurants the bill authorizes, Fiscal Research used information generated per bar and restaurant based on information within the Spectrum reports (specifically, the total estimated GGR of bars and restaurants holding a North Carolina Lottery Commission license to sell lottery products) and applied it to the estimated number of such facilities the bill authorizes. Total estimated GGR was then adjusted to account for growth in population and median household income.

The Spectrum reports assumed that the tax would be based on GGR, without any further deductions. To account for the deductions authorized by the bill, Fiscal Research reviewed tax data from several states that allow one or more deductions that are similar to the deductions

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[7] Spectrum Gaming Group (2020). *Gaming Study: Analysis of Current and Potential New Gaming Activities in North Carolina.*

[8] GGR is defined by the Spectrum reports as "the amount retained after all winning wagers have been paid, but before any expenses or taxes have been deducted." The Spectrum reports provide estimates of North Carolina's GGR both with and without a "first-mover advantage;" which is a term referring to the advantage gained by the first entrant into a market. Sometimes the first-mover advantage can stick, meaning that some customers who have tried the services of the industry pioneer will remain loyal even when other providers enter the market. At the time of the report, sports betting was not in effect in Virginia. Spectrum provided two sets of estimated GGR, one with North Carolina having a first-mover advantage against surrounding states, and a second set without the advantage. Since both Tennessee and Virginia implemented sports betting before North Carolina, FRD relied on Spectrum's GGR estimates without the first-mover advantage.

allowed in the bill. Based on this review, Fiscal Research estimated the total amount of deductions allowed under the bill. Fiscal Research's estimate accounts for the anticipated reduction in the promotional credit deduction given the bill's corresponding phase-out rates starting in 2025 and ending in 2028. Fiscal Research was unable to find any states that allow a comparable deduction for uncollectible receivables. The bill allows for a deduction for uncollectable receivables (sometimes referred to as bad debt), with a maximum deduction of 4% of GWR. States that allow this sort of deduction often apply a much lower cap on the deduction, so Fiscal Research is unable to predict how the higher cap may impact the amount of deductions taken. Based on limited data from several other states, Fiscal Research assumed that the total amount of uncollectable receivables deducted would be only 0.34% of GWR, far less than the maximum allowed in the bill; if uncollectible deductions are closer to the maximum amount allowed by the bill, then the amount of tax revenue generated by the bill may be much lower than estimated in this memo.

Using these adjustments to revenues, Fiscal Research arrived at AGWR figures to be the basis for the tax imposed at the rate of 14%. The table below shows the estimated revenues generated from the privilege tax imposed by the bill.

($ in millions)

Revenue	**FY 2022-23**	**FY 2023-24**	**FY 2024-25**	**FY 2025-26**	**FY 2026-27**
Privilege Tax	$4.69	$8.62	$15.76	$20.32	$22.31

<u>Licensing Fees</u>

The bill assesses licensing fees to identified sports wagering providers as detailed in the table below:

Frequency	**Interactive Sports Wagering License**	**Service Provider License**	**Sports Wagering Supplier License**
Initial License	$1,000,000	$50,000	$30,000
5-Year Renewal	$1,000,000	$50,000	$30,000

The number of interactive sports wagering licenses issued by the Commission are required to be at least 10, but no more than 12 licenses. Based on the experience in neighboring states, this analysis assumes all 12 licenses would be issued over a two-year period in equal quantity (i.e., 6 licenses approved in FY 2022-23, and 6 approved in FY 2023-24).

The number of service provider licenses and sports wagering supplier licenses are unrestricted in the bill and this analysis is unable to estimate the number of licenses of each type that would be issued and their respective timeline of issuance. In order to provide a revenue estimate for service provider licenses and sports wagering licenses, this analysis assumes that a license of each type would track the experience of the issued sports wagering license.

As a result, this analysis estimates licensing fee revenue over the next 6-year period as detailed in the table below:

($ in millions)

Revenue	FY 2022-23	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27	FY 2027-28
License Fees	$6.48	$6.48	$0	$0	$0	$6.48

Estimated licensing fee revenue would be first used to cover administrative expenses of the Lottery Commission associated with sports wagering, with any excess revenue deposited in the General Fund.

Expenditures by North Carolina Lottery Commission

The bill places new administrative requirements on the Commission, including but not limited to:

- Developing and implementing the sports wagering licensing requirements detailed in the bill;
- Conducting background checks of license applicants;
- Auditing sports wager operators upon request; and
- Conducting hearings on licensee violations.

The Commission has estimated that the bill would have one-time implementation costs of approximately $167,000 with an additional recurring cost of $1.345 million to implement the requirements of the legislation. This analysis has examined administrative cost estimates regarding sports wagering activities from Virginia[9] and the income statement from the Tennessee Lottery[10] and finds that the Commission's estimates are reasonable. Therefore, the estimated administrative costs of the Lottery Commission are detailed in the table below:

($ in millions)

Expenditures	FY 2022-23	FY 2023-24	FY 2024-25	FY 2025-26	FY 2026-27
Lottery Commission	$1.512	$1.374	$1.403	$1.435	$1.466

Figures adjusted for inflation based on PCE Price Index projections (Moody's Analytics – December 2021)

Distribution of Revenue

The bill directs that from the total tax revenue, the Department of Revenue shall retain up to $500,000 for its costs in administering the tax, followed by the Lottery Commission to reimburse itself for its expenses in administering the program that are not covered by fee revenue. Of the remaining amount, the first $2 million is dedicated to the Department of Health and Human Services (DHHS) gambling addiction education and treatment programs and $500,000 for the North Carolina Parks and Recreation Authority (NCPRA) to give grants to all 100 counties for youth sports development. Of the remaining amount, 10% is to be distributed equally among seven UNC-constituent institutions, 30% to the North Carolina Major Events, Games and Attractions Fund, and 60% to the General Fund.

TECHNICAL CONSIDERATIONS

N/A.

[9] https://lis.virginia.gov/cgi-bin/legp604.exe?201+oth+HB896FER122+PDF

[10] https://tnlottery.com/wp-content/uploads/2022/02/FY-2021-Financial-and-Compliance-Audit-Report.pdf#page=20

DATA SOURCES

Colorado Department of Revenue; Connecticut State Department of Consumer Protection; gamblingindustrynews.com; Globalnewswire.com; LegalSportsReport.com; Moody's Analytics; National Conference of State Legislatures; North Carolina Education Lottery Commission; North Carolina Office of State Budget and Management; Pennsylvania Gaming Control Board; Play Colorado; Play Michigan; Play Pennsylvania; Spectrum Gaming Group; Sportsbettingdime.com; Sportsbetlistings.com; Tax Foundation; Tennessee Education Lottery; The Florida Lottery; The Virginia Lottery; usbets.com; U.S. Census Bureau; Virginia Department of Planning and Budget; Virginia Lottery.

LEGISLATIVE FISCAL NOTE – PURPOSE AND LIMITATIONS

This document is an official fiscal analysis prepared pursuant to Chapter 120 of the General Statutes and rules adopted by the Senate and House of Representatives. The estimates in this analysis are based on the data, assumptions, and methodology described in the Fiscal Analysis section of this document. This document only addresses sections of the bill that have projected direct fiscal impacts on State or local governments and does not address sections that have no projected fiscal impacts.

CONTACT INFORMATION

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