

Stephen Martino took the helm of the Maryland State Lottery on April 26 of this year. It looks like a perfect fit. Director Martino comes to Maryland with five years of experience as the executive director of the Kansas Racing and Gaming Commission. His role there included the development of the regulatory framework for casino gaming in Kansas and overseeing the opening of the first state-owned casino in the country. Now he gets to shepherd the implementation of casino gaming in Maryland.

The soft economy has required casino developers to adjust revenue projections and build-out strategies. But everything is progressing according to plan. Director Martino's bold leadership style has already been evidenced when challenged to explain why the state should procure top-of-the-line slot machines. Respectful of all interest groups and political constituencies and ever frugal with taxpayer money, Director Martino is committed to holding fast to a strategy that ensures the long-term success of this giant project and delivers maximum benefits to the state of Maryland.

Paul Jason, Public Gaming: *Slight digression before we talk about Maryland. Why should states use casino gambling to subsidize horse-racing? Why not let horse-racing stand or fall on its own and have the state focus on maximizing the profitability of casino gambling?*

Stephen Martino: There are a few obvious reasons. One, the horse-racing industry is struggling and may not survive long-term without help or a new business model. Two, the facilities already process wagering transactions, so they already have some of the systems in place to jump start gaming activity. Three, you're not creating a new gambling footprint, you don't need to build a whole new casino; instead you're just expanding on a facility that's already in place.

Other advantages include the fact that you have a pre-existing customer base, people who know who you are and where you are. So instead of introducing an entirely new product to the marketplace, you're offering an enhanced version of a product that at least some people are familiar with. From a financial point of view, adding casino gaming to a horse-racing facility is less costly than launching a new casino. Expanding on a pre-existing facility like that enables the developer to scale-up in a way that doesn't require as large an upfront payment and as lengthy a payback or ROI period. And you can combine those reasons with the fact that most horse-racing businesses have long historical relationships with the political systems in the state and people don't want them to die.

There was a competitive bidding process in Kansas for the right to operate a casino. How did that work exactly? I don't quite get how racing facilities bid on something they were going to get it anyway.

S. Martino: They did not have to bid. The competitive bidding process was only for the casinos. However, the legislature was keen on preventing the racetrack owners from receiving a wind-fall profit. So the tracks are taxed at a higher rate than casinos. Casinos are taxed 22% and racetracks 40%. The goal was to level the playing field. Racetracks avoid the bidding process but in return are taxed at a higher rate that will likely make it hard for them to compete in the long-term.

And even with the casino side bringing in more customers to the facility, the racing side of the business may still not get into the black, right? So the casino side of the race-track would be paying those higher taxes and potentially be subsidizing the racing part of the business at the same time. Seems problematic.

S. Martino: One track ran greyhounds year round and then also had to operate horse racing. The gaming law required them to double the length of its horse meet in order to get slot machines, and lengthening that meet is an expensive proposition. The answer is that some racetracks will close because the business model just doesn't work. It is challenging to make gaming at a racing facility work when you have profound differences between how a state treats a casino and the racetrack. Every state is different, but markets obey the same economic rules. Tax structures and regulatory frameworks need to be established with that in mind.

The marketplace is infinitely complex. So it would seem imperative that the casino licensing terms, conditions, tax structures, and everything else that is determined in a political process somehow get aligned with a dynamic marketplace that doesn't play politics. It does not seem like state legislatures appreciate that.

S. Martino: Oh, I think they do understand and appreciate it. Keep in mind that gambling



Stephen Martino

Director of the Maryland State Lottery

legislation and laws that authorize the expansion of gaming come out of a political process. That process typically includes different interest groups that have their own, oftentimes opposing, opinions on what they want the end result to be. Negotiation leads to compromise in order to reach a consensus. However, often what you end up with is not going to be a perfectly rational law to implement. Sometimes there are people whose heartfelt beliefs are not supportive of gambling under any circumstance or for any cause. Sometimes the end result includes provisions that are decidedly counter-productive for everyone. But I don't tend to think it's because people are not mindful of the need for alignment as you described it. Often, incongruities or difficulties in the law represent what had to be done to develop a consensus among interest groups and get passage. Licensing terms, conditions, regulatory frameworks and tax structures are all subject to this political process. The legislative process can be messy, but we shouldn't criticize legislators for

doing what they have to do to make the system work and get things done. Likewise, regulators need to reconcile pieces of legislation that don't always fit together well.

You referred to the criticism that came out about the cost of the slot machines here in Maryland. First and foremost, that was a product of some misleading reporting. The press was developing costs for machines that were wrong. Taken on face value the way it was reported, it's quite understandable that people would be upset because it appeared that we were paying more for slot machines than commercial gaming operators in other states. Our contracts bundled the cost of maintenance over five years with the purchase of the machines. It is a format required by state procurement law and in the end costs no more than if you break service and maintenance costs out separately. Once we disseminated the information and clarified the issue, people understood that we negotiated competitive pricing and terms with our commercial partners. But the larger point is that the legislature wanted the Lottery to be the owner of slot machines in the state's casinos. There was not an outcry about this by legislators because we were implementing the law they passed. It was just a poorly reported story. Laws pertaining to gambling are imperfect because they are the result of competing forces that come to agreement through compromise. I don't know of any jurisdiction where gambling legislation was passed with unanimous approval.

So the political process may not be efficient and the resulting legislation imperfect. But that's the way America works and we should feel good about that.

S. Martino: I think that's right. Our job as lottery directors, regulators and public servants is to implement the policies to the best of our abilities and to be respectful of the process and the elected officials who are doing their best to translate the will of the people into sound public policy.

Maryland voters approved the casino gaming plan almost two years ago. Why does it take so long to implement a casino gaming agenda?

S. Martino: In my opinion, the idea that this is taking too long is yet another myth. The referendum allowing the state to implement gaming was passed in November 2008. Nothing could be done prior to the vote of the people to move the gaming expansion process along. We are looking to open our first casino at the end of September. That's 22 months to go from zero to up and running. That included a competitive bid process, the construction of the casino and

installation of facility infrastructure and acquisition of games. These things all take time and making it happen in less than two years is a respectable timeframe. In Kansas, it took two and a half years from passage of the legislation to the first casino opening in Dodge City. I think when you look at other states, they all took a similar amount of time. These things take time if done properly and responsibly.

Makes sense when you explain it that way. Specifically, what is the timeline for the build out of your casinos? How many are there and when do you expect them to turn on the first slot machines?

S. Martino: There are five casinos authorized for Maryland. Three licenses have been granted through a competitive bidding process. Penn National is scheduled to open its Hollywood Casino in Perryville, Maryland, on Sept. 30. We hope Ocean Downs, which is close to Ocean City on the Eastern Shore, will open by the end of the year. The third license has been granted to the Cordish Company to build a casino at the Arundel Mills Mall. That license has been tied up in the courts. The Maryland Court of Appeals, which is the state's highest court, decided in August that it is going to allow a referendum on the zoning for the casino. So that will go before the voters in November. If the voters uphold the zoning, that casino will go forward. And if the voters reject the zoning, then we might very well be back at square one. Then there are two other authorized casinos. One is in Western Maryland in Allegany County at a state-owned resort hotel called Rocky Gap. The RFP to operate the casino there was issued July 21. The responses are due back on November 9th. So we should know then how many people are bidding. The final authorized casino is for Baltimore City. That's gone through one round of competitive bidding. The applicant was rejected, has sued the city and the state, and so we're before various administrative boards and the courts on that. We don't know right now when an RFP for the Baltimore facility might be issued.

On the Cordish Arundel Mills project, did you say that it's subject to a local referendum?

S. Martino: It is. The Anne Arundel County Commission already approved it, but now it is being put to a vote of the people. A lower court struck it down and said the petition to put this to a referendum was unconstitutional. But it was appealed to the Maryland Court of Appeals, and they ruled in August that it was constitutional to have that county-wide referendum. And so it will be on the ballot in November.

The new electronic games/VLTs/slots deliver so much more entertainment value than ever before, don't they? With the intense competition in this region, I would think there is no better ROI than a product that is most likely to attract the customers. And no worse ROI than to invest in a legacy product that wouldn't attract a customer.

S. Martino: Yes, but it's not just a matter of buying the most expensive machines because they are supposedly better. You need an appropriate mix of machines. Maryland will have a good mix of slot machines at its casinos. Some are so-called "high-end", but it's not necessary or even desirable to have all machines be similar playing experiences. Many people enjoy the more basic slot machine. The state of Maryland is buying the slot machines. You'd think the casino operator would prefer the high-end machines since they don't pay for them. But even the casino operator prefers to have a diversity of product on the floor to appeal to the broadest range of player preferences. We get outside viewpoints, apart from the casino operator and the slot manufacturers, to ensure we have the cutting-edge technology and game content that attracts the players. Our objective is to maximize long-term ROI by having the optimal mix of lower cost as well as higher-end machines. But we also need to negotiate the very best deal for the state. The state retains 67% of the gross gaming revenue, so it is in our interest to invest in the machines that will attract the players and generate maximum revenues.

Casino gaming will constitute another gaming option for the consumer. Will that cut into traditional lottery revenues and what can be done to mitigate the negative impact?

S. Martino: I do not think casino gaming will have a significant impact on traditional lottery revenues. You have to keep in mind that casino gambling has been within a couple hours drive of Maryland for years, in places like Delaware and West Virginia. So, whatever impact casino gaming has on traditional lottery has largely already occurred. The Maryland Lottery just reported our 13th straight year of record-breaking sales and we are confident that having our own casinos in Maryland will not change that positive trend-line. Opening our own casinos will just re-direct the gaming revenues that were leaving the state to come back to Maryland.

I would think that legislators in all states would see it that way. Do you have any thoughts on the ways of cross promoting between the different gaming cat-

egories? Would you anticipate promoting traditional lottery in the casinos and/or vice-versa?

S. Martino: Yes. Penn National is going to be a Maryland Lottery retailer. So we will be selling traditional lottery products in the casino's retail space and through instant ticket vending machines (ITVMs). We believe that's going to be a good revenue generator for us. We are going to have a conversation with Penn after they open about adding our monitor games, Keno and Racetrax. Cross-promoting in the other direction, running casino gaming promotions through our retailers, will be more challenging. But we are kicking around some ideas. I think once all the facilities are open we will be able to explore ways to cross promote in both directions in a more coordinated fashion. In the meantime, there will be a prominent Maryland Lottery presence in the casinos when they open.

What kinds of second-chance drawings or other Internet-based marketing initiatives does Maryland Lottery do?

For the second year in a row, we are proud to partner with the Baltimore Ravens to offer the Ravens Cash Fantasy scratch-off. Last year's Ravens Cash Fantasy was the best-selling \$5 scratch-off ever sold by the agency. The ticket features three instant top prizes of \$1 million. The ticket also features an Internet Promotion. Players enter the EXTRA YARDS from the perforated portion of the ticket at mdlotttery.com/ravens. The accumulated yards can be used to enter drawings for incredible football-themed prizes such as Ravens season tickets for life, season tickets for 2010 or 2011, an away trip with

the team and the chance to hang out on the sidelines during a Ravens game. Some lucky player will even score a trip to NYC for the Ravens Draft Day Party. There are numerous other prizes as well, from autographed footballs, photos and mini-helmets to framed jerseys and more.

Another exciting second-chance contest going on right now is our Reese's scratch-off "Hit It Here" promotion. This is in affiliation with the Baltimore Orioles and offers the shot at winning up to \$100,000. Players just have to mail in two non-winning Reese's scratch-off tickets for the chance to be chosen as a Fan of the Game. A Fan of the Game is then randomly selected for each 2010 Orioles home game. If an Orioles player hits a home run that hits the Maryland Lottery "Hit it Here" sign located past the left centerfield fence, the Fan of the Game wins \$100,000. If it doesn't hit the sign, the Fan of the Game wins \$100 worth of Reese's scratch-off tickets along with entry into the Grand Prize drawing for a trip-for-two to Orioles Spring Training 2011 in Sarasota, Florida. Judging by the amount of entries, players seem to love the second-chance contests. The added opportunities to win are not only popular with our loyal players, but appear to be attracting new players to the Maryland Lottery as well.

There seems to be a lot of flexibility to create new and different games and promotions using the second-chance drawing concept.

S. Martino: There is. The real luxury of second-chance contests is that they allow you to be innovative. Tying in to sports

teams is a natural in ways that don't work nearly as well with the printed scratch ticket. But giving the player an additional chance without an extra cost to win is like doubling the value proposition. So it's not surprising that the players enjoy it.

And building an Internet-based relationship with your customer. Don't you think the Internet enables a whole new way of interacting with your players?

S. Martino: It does. We are getting ready to launch a redesigned Website, using blogs, Facebook, Twitter and Flickr. We are going all in to generate excitement about social media opportunities and to connect with our players and enable them to connect with each other.

One of the things we're dealing with is a dramatic cut to our advertising budget during the last four or five years. We expect our investment in Internet initiatives to deliver a far better ROI than most traditional forms of advertising, and so that's one thing we're seeking. We intend to use the Internet to keep our image fresh, new and exciting with the players. We'll be trying new things but also just jazzing up the way we display the traditional games like Pick 3 and Pick 4, PowerBall and Mega Millions to make those more accessible for the core players.

I do want to add that we are very mindful of the need for effective Responsible Gaming tools. As we move into new media like Internet and mobile, we need to guarantee that age restriction mechanisms work effectively and that our players enjoy a responsible gaming play style. ♦