

Performance Audit Report

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**Video Lottery Operation Licensees  
Minority Business Participation**

October 2016

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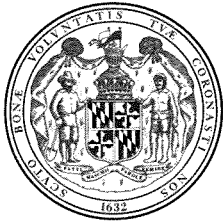
**OFFICE OF LEGISLATIVE AUDITS**  
**DEPARTMENT OF LEGISLATIVE SERVICES**  
**MARYLAND GENERAL ASSEMBLY**

**For further information concerning this report contact:**

**Department of Legislative Services  
Office of Legislative Audits**  
301 West Preston Street, Room 1202  
Baltimore, Maryland 21201  
Phone: 410-946-5900 · 301-970-5900  
Toll Free in Maryland: 1-877-486-9964  
Maryland Relay: 711  
TTY: 410-946-5401 · 301-970-5401  
E-mail: [OLAWebmaster@ola.state.md.us](mailto:OLAWebmaster@ola.state.md.us)  
Website: [www.ola.state.md.us](http://www.ola.state.md.us)

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DEPARTMENT OF LEGISLATIVE SERVICES  
OFFICE OF LEGISLATIVE AUDITS  
MARYLAND GENERAL ASSEMBLY

Warren G. Deschenaux  
Executive Director

Thomas J. Barnickel III, CPA  
Legislative Auditor

October 19, 2016

Senator Guy J. Guzzone, Co-Chair, Joint Audit Committee  
Delegate C. William Frick, Co-Chair, Joint Audit Committee  
Members of Joint Audit Committee  
Annapolis, Maryland

Ladies and Gentlemen:

As required by Section 9-1A-34 of the State Government Article of the Annotated Code of Maryland, we audited the information submitted to the Maryland Lottery and Gaming Control Commission (MLGCC) through the Governor's Office of Minority Affairs (GOMA) by video lottery operation licensees on the attainment of minority business participation goals, and the licensees' efforts to maintain those goals. Our performance audit covered the licensees' construction and procurements for the Hollywood Casino Perryville, the Casino at Ocean Downs, the Maryland Live! Casino, the Horseshoe Casino Baltimore, the Rocky Gap Casino Resort, and the MGM National Harbor Casino for calendar year 2014.

Our evaluation of the video lottery terminal (VLT) information, which included minority business participation data received directly from the licensees or GOMA, indicated that the information published by GOMA in its 2014 MBE compliance report, dated September 30, 2015, was generally accurate and complete. MLGCC used the information provided by GOMA in preparing its annual report, dated October 30, 2015, for calendar year 2014 on the VLT facilities' participation activity. MLGCC audited the VLT information received directly from the licensees and GOMA to verify the information that was included in its annual report.

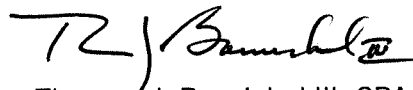
As of June 30, 2016, of the 18 amended minority participation goals to be established for the 6 video lottery terminal licensees, 10 had been established, 5 were in the process of being established, and no action had been taken on 3 (for which there was no related expenditure activity during calendar year 2014). For the 5 in process, MLGCC had completed its necessary tasks for establishing 4 of these goals, but was waiting for information from the Maryland Department of Transportation (MDOT) to

finalize the goal setting process. Under the approved Maryland goal setting process, MDOT is responsible for applying a proprietary goal-setting formula, and submitting the resultant proposed goals to MLGCC for approval. For the other goal, MLGCC was still gathering or reviewing information from the licensees prior to preparing its submission to MDOT.

Chapter 49, 2016 Laws of Maryland, eliminated the requirement that the Office of Legislative Audits annually audit and evaluate the information submitted by licensees to MLGCC. Consequently, this is the final audit report to be issued on the attainment of minority business participation goals by video lottery operation licensees, and their efforts to maintain those goals. Nevertheless, the attainment of goals will be subject to audit and evaluation during this Office's regularly required fiscal compliance audits of MLGCC, conducted in accordance with Section 2-1220 (a) (2) of the State Government Article.

MLGCC's response to this audit is included as an appendix to this report. Since there are no recommendations in this report related to GOMA, a written response from GOMA was not necessary. We wish to acknowledge the cooperation extended to us during our audit by MLGCC and GOMA.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "TJ Barnickel III", with a stylized flourish at the end.

Thomas J. Barnickel III, CPA  
Legislative Auditor

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\* Denotes item repeated in full or part from preceding audit report

## **Background Information**

### **Video Lottery Facilities**

The General Assembly passed legislation to license video lottery terminal (VLT) gaming in Maryland at six locations in the State (Anne Arundel County, Baltimore City, Cecil County, Allegany County, Worcester County, and Prince George's County). Current law authorizes 16,500 VLTs with a maximum of 4,750 VLTs at any one location, and allows VLT licensees to operate certain table games such as roulette, baccarat, blackjack, and poker. VLT equipment is owned or leased by either the Maryland Lottery and Gaming Control Commission (MLGCC) or the VLT licensees.

The video lottery operation licenses required by law to operate a VLT facility were awarded by the Video Lottery Facility Location Commission. The MLGCC oversees VLT facility operations, and is required to ensure that licensees comply with the regulatory framework of the VLT program, including minority business participation.

### **Minority Requirements Studies**

Section 4 of Chapter 4, Special Session, and Laws of Maryland 2007 required the Maryland Department of Transportation (MDOT), in consultation with the General Assembly and the Office of the Attorney General, to initiate two studies to evaluate the continued compliance of the minority participation requirements of Section 9-1A-10 of the State Government Article with any federal and constitutional requirements. The studies were also to evaluate race-neutral programs or other methods that could be used to address the needs of minority investors and minority businesses. The first study was submitted to the Legislative Policy Committee by the Secretary of MDOT with a letter (dated August 9, 2011), to address the aforementioned Special Session requirements. In response to the completion of the first study, the Attorney General of Maryland advised on August 11, 2011 that a minority business participation program for VLT licensees could now be implemented in compliance with the VLT law.

The report of the second study was due to the Committee by September 30, 2013. In a letter dated November 20, 2013, the Secretary of MDOT notified the Legislative Policy Committee that the second study would not be completed. The letter stated that the 2011 study fulfills the obligations for the studies outlined in the law.

## **Minority Participation Requirements**

Section 9-1A-10 of the State Government Article of the Annotated Code of Maryland specifies that, for construction and procurements related to the operation of VLTs, video lottery operation licensees must meet, at a minimum, the same minority participation requirements specified for State agencies in Title 14, Subtitle 3 of the State Finance and Procurement Article. According to this law, if the Governor's Office of Minority Affairs (GOMA) reports that a licensee is not in compliance with the minority participation requirements, MLGCC may take immediate action to ensure compliance of the licensee.

The request for proposals (RFP) issued in December 2008 by the Video Lottery Facility Location Commission delineated the minority participation goals, with overall goals of 25 percent for Allegany, Cecil, and Worcester counties, and 35 percent for Anne Arundel County and Baltimore City, and sub-goals for African-American and women-owned businesses. However, because of constitutionality issues, the Attorney General advised, on August 11, 2011, that the RFP provisions relating to these goals needed to be amended to set separate goals for each VLT facility and, where appropriate, for each separate contract of significant duration, scope, and size entered into by licensees. This advice also stated that these goals need to be based on the availability of minority businesses to perform the work at each location, and waivers must be available for instances in which a licensee is unable to meet the goals after making good faith efforts.

To address the requirements and prior legal concerns noted in the Attorney General's August 2011 memorandum, MLGCC worked collaboratively with other State agencies and stakeholders, including GOMA and MDOT, to develop an amended Minority Business Enterprise (MBE) goal-setting process. MDOT's current role in the goal-setting process is to apply a proprietary goal-setting formula, that had been developed in 2013 by a consultant, under contract with the State. The results from applying this formula are then submitted by MDOT to MLGCC, which is responsible for formally adopting and notifying VLT licensees of the actual goals.

## **Status of Licenses**

For each casino, Table 1 provides the dates that the license was awarded and when VLT gaming operations began. In accordance with Section 9-1A-04 of the State Government Article of the Annotated Code of Maryland, MLGCC granted MGM National Harbor (MGM) in Prince George's County two six-month extensions to begin its VLT gaming operations; MGM is now required to open no later than February 14, 2017.

**Table 1**  
**Video Lottery Facility License and Operations Data**

Casino	Local Jurisdiction	Date License Awarded	Date Operations Began
Hollywood Casino Perryville	Cecil	10/21/2009	9/27/2010
Casino at Ocean Downs	Worcester	9/23/2009	1/4/2011
Maryland Live! Casino	Anne Arundel	12/7/2009	6/6/2012
Rocky Gap Casino Resort	Allegany	4/26/2012	5/22/2013
Horseshoe Casino Baltimore	Baltimore City	7/31/2012	8/26/2014
MGM National Harbor	Prince George's	8/14/2014	Future

**Source:** Governor's Office of Minority Affairs September 30, 2015 MBE Compliance Report and MLGCC Licensee Information

### **Governor's Office of Minority Affairs (GOMA)**

Section 9-1A-10 of the State Government Article of the Annotated Code of Maryland requires GOMA to monitor licensees' compliance with minority business participation requirements and to report at least every six months to the MLGCC on the licensees' compliance with the requirements. MLGCC uses the information obtained from GOMA to prepare an annual report to the Governor and the General Assembly on the attainment of the minority business participation goals by the licensees and their efforts to maintain those goals. MLGCC's report for calendar year 2014 was issued on October 30, 2015.

### **Status of Findings From Preceding Audit Report**

Our audit included a review to determine the status of the three findings contained in our preceding audit report, dated April 5, 2016. We determined two of these findings were satisfactorily addressed. The remaining finding is repeated in this report, although progress was made by MLGCC to address the issue.



## Audit Scope, Objectives, and Methodology

### Scope and Objectives

Section 9-1A-34 of the State Government Article of the Annotated Code of Maryland required the Office of Legislative Audits to annually audit and evaluate the information submitted by video lottery operation licensees to the Maryland Lottery and Gaming Control Commission (MLGCC) on the attainment of minority business participation goals specified for construction and procurements related to their operations and the efforts to maintain those goals. We conducted a performance audit to assess the accuracy of the calendar year 2014 information reported by the six video lottery operation licensees identified in Table 2.

<b>Table 2</b> <b>Licensee VLT Data as of December 31, 2014</b>			
<b>Licensee</b>	<b>Casino</b>	<b>Maximum Number of VLTs Initially Approved</b>	<b>Number of VLTs Approved as of 12/31/14</b>
Penn Cecil Maryland, Inc.	Hollywood Casino Perryville	1,500	850
Ocean Enterprise 589, LLC	Casino at Ocean Downs	800	800
PPE Casino Resorts Maryland, LLC	Maryland Live! Casino	4,750	4,222
Evitts Resort, LLC	Rocky Gap Casino Resort	850	577
CBAC Gaming, LLC	Horseshoe Casino Baltimore	3,750	2,500
MGM National Harbor, LLC	MGM National Harbor	3,600	3,600

**Source:** MLGCC Licensee data reports

Our audit was performed in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objectives. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objectives.

## **Methodology**

To accomplish our objectives, we interviewed employees of the licensees, MLGCC, and the Governor's Office of Minority Affairs (GOMA). We reviewed GOMA's and MLGCC's data collection process and reporting. We also evaluated the minority participation calculations for accuracy, and reviewed and tested the records of the licensees, including contractor classifications, expenditure data, invoices, and reports of minority participation levels.

Our fieldwork was completed during the period from October 2015 through July 2016. A copy of the draft report was provided to MLGCC and GOMA. MLGCC's responses to our findings and recommendations appear as an appendix to this report. Since there were no recommendations made to GOMA, it did not submit responses to this report. As prescribed in State Government Article, Section 2-1224 of the Annotated Code of Maryland, we will advise MLGCC regarding the results of our review of its responses.

Finally, Chapter 49, 2016 Laws of Maryland, eliminated the requirement that the Office of Legislative Audits annually audit and evaluate the information submitted by licensees to MLGCC. Consequently, this is the final audit report to be issued on the attainment of minority business participation goals by video lottery operation licensees, and their efforts to maintain those goals. Nevertheless, the aforementioned MLGCC responses and the attainment of goals will be subject to audit and evaluation during this Office's regularly required fiscal compliance audits of MLGCC, conducted in accordance with Section 2-1220 (a) (2) of the State Government Article.

## Conclusions

As of June 30, 2016, 10 of the 18 VLT minority participation goals had been established, and certain actions have been taken to establish most of the remaining goals. Without properly established goals, the Maryland Lottery and Gaming Control Commission (MLGCC) will be unable to encourage and assess licensee achievement of those goals, or for a licensee failing to achieve those goals, take appropriate action to ensure compliance.

MLGCC was in the process of establishing an additional five amended minority participation goals for five video lottery terminal licensees (including four goals for four of the video lottery terminal licensees that incurred expenditures in calendar year 2014). MLGCC had taken no action to establish the remaining three goals, but there was no reported calendar year 2014 expenditure activity related to these specific goals.

For the five goals in process, MLGCC had completed the necessary tasks to establish four of these amended goals, and had submitted the information to the Maryland Department of Transportation (MDOT). MDOT is responsible for applying a proprietary goal-setting formula, on which the goals are based, and submitting the amended participation goals to MLGCC for final approval. For the other goal, MLGCC was gathering and verifying licensee information prior to submission to MDOT. Table 4 presents the status of all 18 goals as of June 30, 2016.

Our evaluation of the video lottery terminal (VLT) information, which included minority business participation data received directly from the licensees or Governor's Office of Minority Affairs (GOMA), indicated that the information published by GOMA in its 2014 MBE compliance report, dated September 30, 2015, was generally accurate and complete. We also found that GOMA had a process in place to review the VLT information received directly from the licensees to ensure that the licensees' information was complete and accurate. MLGCC used the information provided by GOMA in preparing its annual report, dated October 30, 2015, for calendar year 2014 on the VLT facilities' participation activity. MLGCC audited the VLT information received directly from the licensees and GOMA to verify the information that was included in its annual report to the Governor and General Assembly. Neither MLGCC's and GOMA's reviews of the submitted licensee information nor our audit disclosed any related findings that warranted mention in this report. Table 3 includes a summary of the applicable licensee submitted information.

<b>Table 3</b> <b>GOMA Reported Minority Participation For Calendar Year 2014</b>				
<b>Casino</b>	<b>Type of Activity Reported</b>	<b>Net Expenditures to All Vendors For Period Reported</b>	<b>Total Expenditures to MBEs for Period Reported</b>	<b>Licensee MBE Participation For Period Reported</b>
Hollywood Casino Perryville	Operations	\$6,332,120	\$320,385	5.06%
Casino at Ocean Downs	Architectural/Engineering	\$737,555	\$89,490	12.13%
	Operations	\$6,555,087	\$700,229	10.68%
Maryland Live! Casino	Operations	\$82,943,029	\$14,048,209	16.94%
Rocky Gap Casino Resort	Operations	\$6,915,437	\$81,644	1.18%
Horseshoe Casino Baltimore	Architectural/Engineering	\$3,523,648	\$199,081	5.65%
	Construction	\$184,183,126	\$66,222,746	35.95%
	Operations	\$16,065,196	\$2,979,114	18.54%
MGM National Harbor	Architectural/Engineering	\$25,594,121	\$7,962,465	31.11%
	Construction	\$72,423,720	\$16,692,627	23.05%

Source: GOMA and MLGCC

Since the Horseshoe Casino Baltimore began operations on August 26, 2014, the “Operations” financial activity reported in Table 3 is not for a full calendar year. Also, on December 23, 2013, the Video Lottery Facility Location Commission awarded a VLT license to MGM National Harbor, LLC. The “Architectural/Engineering” and “Construction” activity shown in Table 3 for this casino, as disclosed by GOMA in its report, includes both calendar years 2013 and 2014. Both years were included because calendar year 2013 was not previously included in GOMA’s report for that year.

## Findings and Recommendations

### Establishment of Minority Participation Requirements

#### **Finding 1**

**Certain amended minority participation goals for five of the video lottery terminal licensees with related calendar year expenditures were not yet established.**

#### **Analysis**

Certain amended calendar year 2014 minority participation goals had not been established for five video lottery terminal (VLT) licensees; including four goals for which there were calendar year 2014 expenditures. Each of the six licensees should have three goals established – one each related to architectural/engineering, construction, and operational procurement activities, resulting in a total of 18 goals. As of June 30, 2016, 10 goals had been established, 5 goals were in process, and 3 goals (for which there was no calendar year 2014 financial activity) had not been established. See Table 4 for a status of the goals by licensee and activity type.

For the five goals in process as of June 30, 2016, the Maryland Lottery and Gaming Control Commission (MLGCC) had completed the necessary tasks in its efforts to establish four, including the operational/procurements goals for four of the licensees. Specifically, MLGCC requested licensees to provide certain budgetary data that was necessary to the goal setting methodology formula, which MLGCC verified for accuracy upon receipt from the licensees. For those four, MLGCC submitted the related licensee data and additional information required by the goal setting methodology to the Maryland Department of Transportation (MDOT). Under an agreement between MLGCC, GOMA and MDOT, MDOT is responsible for applying a proprietary goal-setting formula, on which the goals are based, and submitting the amended participation goals to MLGCC for final approval. We found that MLGCC was working on gathering or verifying licensee data for the other goal, but that data was not fully ready for submission to MDOT.

**Table 4**  
**Summary – Calendar Year 2014 Video Terminal Licensee Goals**  
**as of June 30, 2016**

Casino	Licensee Activity Type (Goal expressed as a percentage of expenditures and date goal was established or goal status)		
	Architectural and Engineering	Construction	Operational Procurements <sup>①</sup>
Hollywood Casino Perryville	Not Established <sup>②</sup>	Not Established <sup>②</sup>	Not Established (Pending at MDOT)
Casino at Ocean Downs	23% (June 20, 2016)	18% June 20, 2016	Not Established (Pending at MDOT)
Maryland Live! Casino	19% (May 30, 2014)	Not Established <sup>②</sup>	Not Established (Pending at MDOT)
Rocky Gap Casino Resort	12% (November 30, 2015)	17% (November 30, 2015)	Not Established (Pending at MDOT)
Horseshoe Casino Baltimore	22% (May 30, 2014)	24% (May 7, 2013)	20% (August 25, 2014)
MGM National Harbor	19% (June 4, 2014)	26% (December 5, 2014)	Not Established <sup>②</sup> (In process at MLGCC)

**Source:** MLGCC and prior OLA audit report

- ① - There were calendar year 2014 expenditures related to the four goals “Pending at MDOT” as of June 30, 2016.
- ② - Activity type did not have any calendar year 2014 expenditures.

Although State law requires VLT licensees to meet the same minority participation requirements specified for State agencies, the Attorney General of Maryland formally advised in August 2011 that, to address constitutionality issues, MLGCC should amend the goals to set separate goals for each licensee, and perhaps for each contract, and consider the proposed contract work and the availability of minority businesses to perform the work.

A similar condition was commented upon in our two preceding audit reports, in which we commented that certain goals had not been established, although MLGCC was committed to establishing all necessary goals.

**Recommendation 1**

**We recommend that MLGCC establish amended minority participation goals for all categories in which VLT licensees have expenditures (repeat).**

## APPENDIX

# Maryland Lottery and Gaming Control Agency

Larry Hogan, Governor • Gordon Medenica, Director



Montgomery Park Business Center  
1800 Washington Blvd., Suite 330  
Baltimore, Maryland 21230

Tel: 410-230-8800  
TTY users call Maryland Relay  
www.mdlottery.com

October 18, 2016

### SENT VIA EMAIL & REGULAR MAIL

Mr. Thomas J. Barnickel III, CPA, Legislative Auditor  
ATTN: Jonathan H. Finglass, CPA, Senior Auditor  
Office of Legislative Audits  
301 West Preston Street, Room 1202  
Baltimore, MD 21201

*RE: MLGCC's Response to Audit Report*

Dear Mr. Barnickel:

Enclosed is the Maryland Lottery and Gaming Control Commission's (MLGCC) response to the Video Lottery Operation Licensees - Minority Business Participation Audit Report for the period January 1, 2014 through December 31, 2014.

If you should have any questions or require additional information, please contact James Butler, Director of Legislative & Policy Affairs, Maryland Lottery and Gaming Control Agency (MLGCA) at (410) 230-8781 or [jbutler@maryland.gov](mailto:jbutler@maryland.gov).

Sincerely,

Gordon Medenica  
Director

Enclosure

cc: Kimberly Robertson Pannell, Chair, Maryland Lottery and Gaming Control Commission  
Gina M. Smith, Deputy Director & Chief Finance Officer, MLGCA  
James Nielsen, Assistant Deputy Director & Chief Operating Officer MLGCA  
Robert T. Fontaine, Principal Counsel, MLGCA  
Michael A. Eaton, Director of Audit and Regulatory Compliance, MLGCA  
James B. Butler, Director, Legislative and Policy Affairs, MGLCA



**Maryland Lottery and Gaming Control Commission (MLGCC)  
Response to Audit Report on Video Lottery Operation Licensees -  
Minority Business Participation for Calendar Year 2014**

**Establishment of Minority Participation Requirements**

**OLA Finding**

**Certain amended minority participation goals for five of the video lottery terminal licensees with related calendar years expenditures were not yet established.**

**OLA Recommendation:**

We recommend that MLGCC establish amended minority participation goals for all categories in which VLT licensees have expenditures (repeat).

**MLGCC Response:**

MLGCC agrees with the recommendation to establish amended Minority Business Enterprise (MBE) participation goals for all categories in which VLT licensees have expenditures. MLGCA will continue monitoring the goal-setting process to ensure that amended MBE participation goals are established for all categories in which VLT licensees have current expenditures.

AUDIT TEAM

**Raymond G. Burton, Jr., CPA, CFE**  
Audit Manager

**Jonathan H. Finglass, CPA**  
Senior Auditor

**Timothy S. Rice**  
Staff Auditor