

Contract Extension with IGT 2019-H 6266

Staff Presentation to the House Finance
Committee
September 24, 2019

Summary

- *2019-H 6266* authorizes extension of current 20-yr Lottery contract with IGT
 - Exclusive provider of lottery services
 - Traditional lottery products
 - Casino related services
 - Excludes Sports Betting
 - Sets framework of terms
 - Upfront payment and minimum investments
 - Commission amounts
 - Jobs commitment

Summary

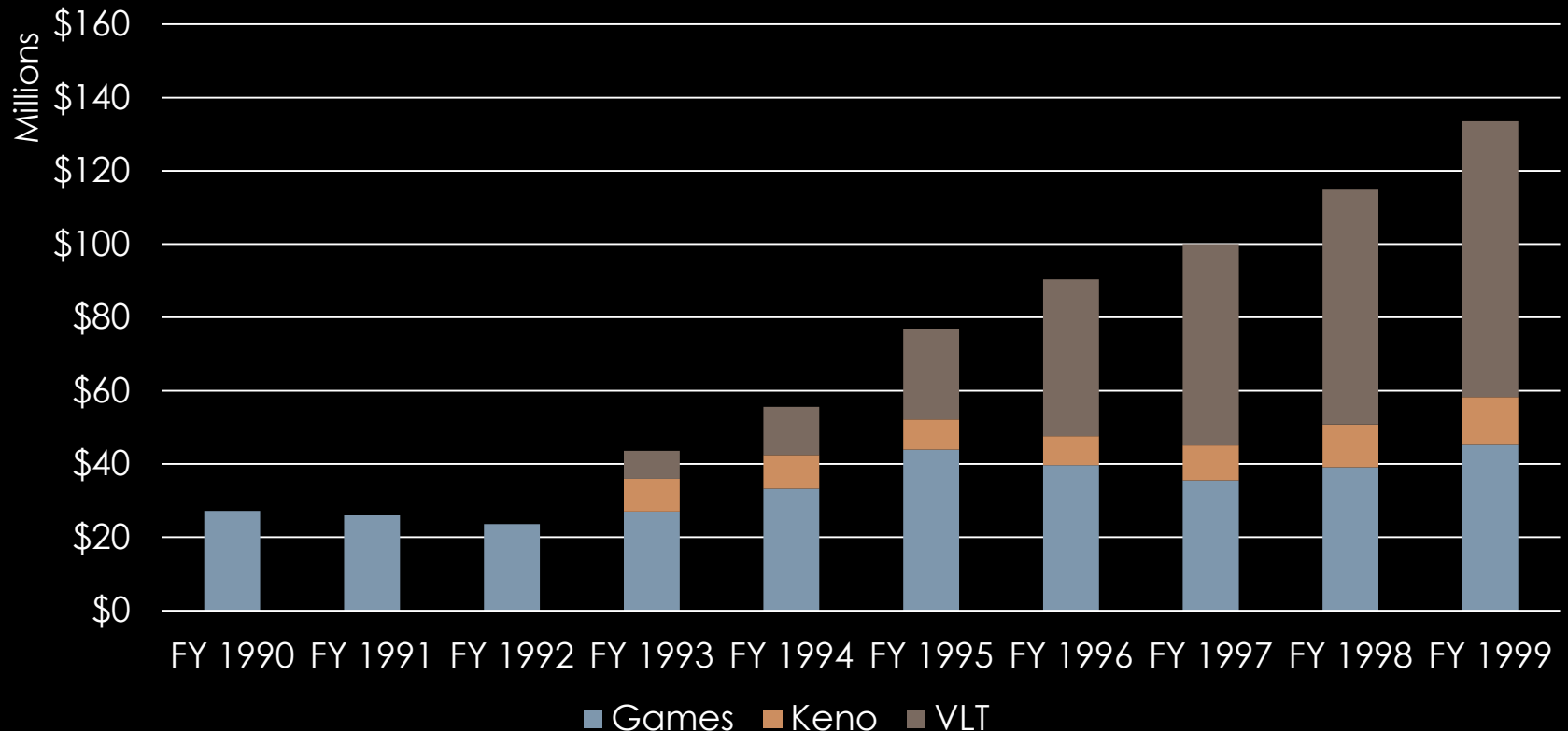
- **Background**
 - **Lottery**
 - **Original Contracts**
 - **Other Changes**
- **Scope of Services**
- **Other Considerations**

Background

- Voters authorized lottery in 1973
- Lottery Commission established in 1974 as a 9-member entity governing lottery operations which were run by a director
 - 3 Senators & 3 Representatives (at least 1 each from minority party)
 - 3 public members appointed by Governor
- Video lottery (slot) machines authorized in 1992

Background

**Lottery Revenues
FY 1990 – FY 1999**



Background

- 2003 General Assembly amended the statutes to allow the Lottery Commission to enter a multi-year “Master Contract” with GTECH
 - Build and maintain its global corporate headquarters in Providence
 - Expand in-state manufacturing operations
 - Maintain 1,000 jobs
 - Incorporated provisions of three existing contracts

Background

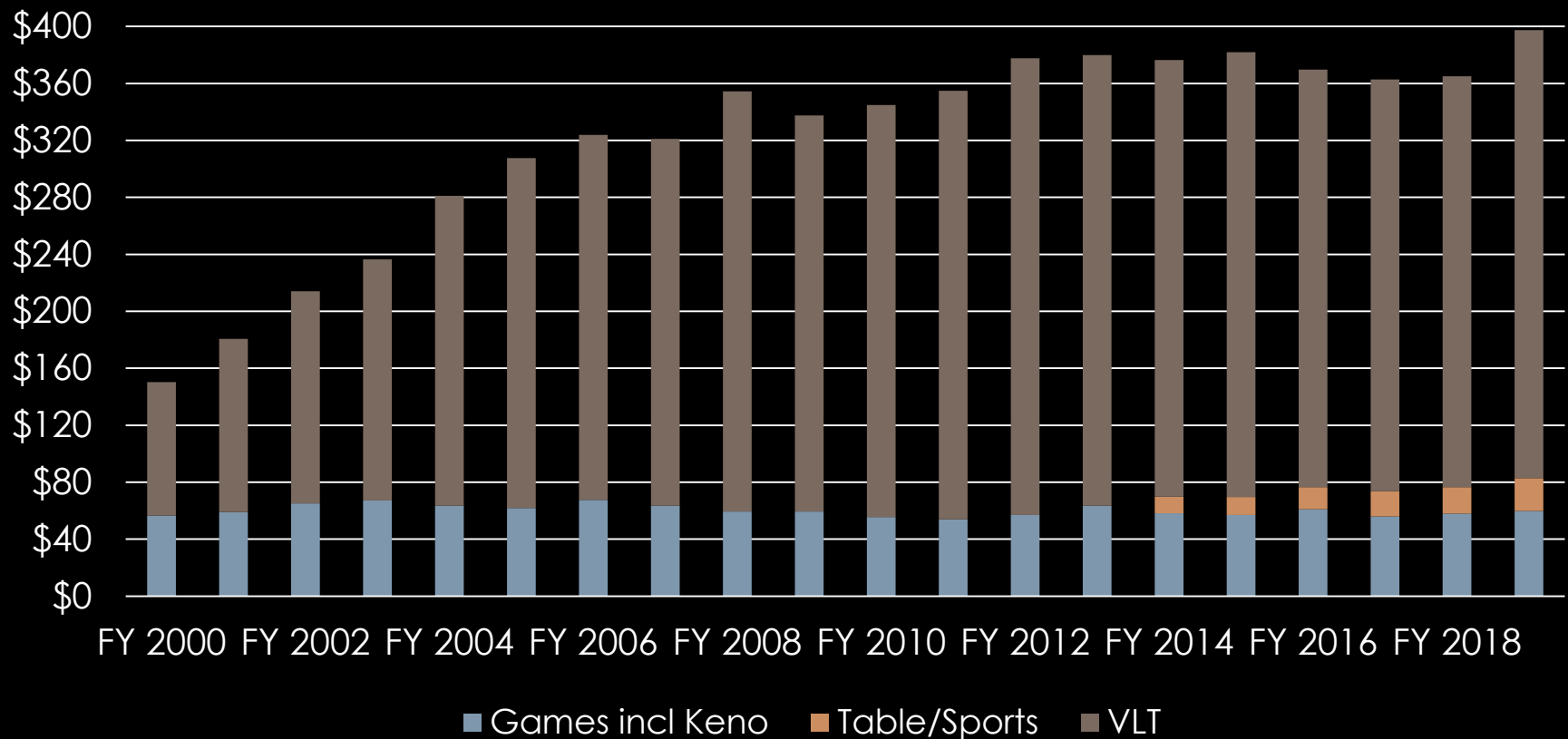
- 2003 master contract incorporated provisions of three active contracts
 - On-Line Lottery Agreement
 - RFP issued in 1996, GTECH only bidder
 - Effective 1997 – 2002
 - Amended 4 times through 2002
 - Video Lottery Agreement
 - RFP issued in 2001, GTECH only bidder
 - 5 year term
 - VLT Agreement
 - 38 month agreement to be a VLT provider

Background

- 2005 Assembly made major changes affecting the Lottery & its revenues
 - Lottery put under Executive Branch control
 - Legislation carrying out separation of powers
 - Long term contracts authorized for facility license holders at both Lincoln & Newport
 - Minimum capital investment requirements
 - Minimum job levels
 - Expansion of VLT machine count
 - Long term commitment on revenue splits

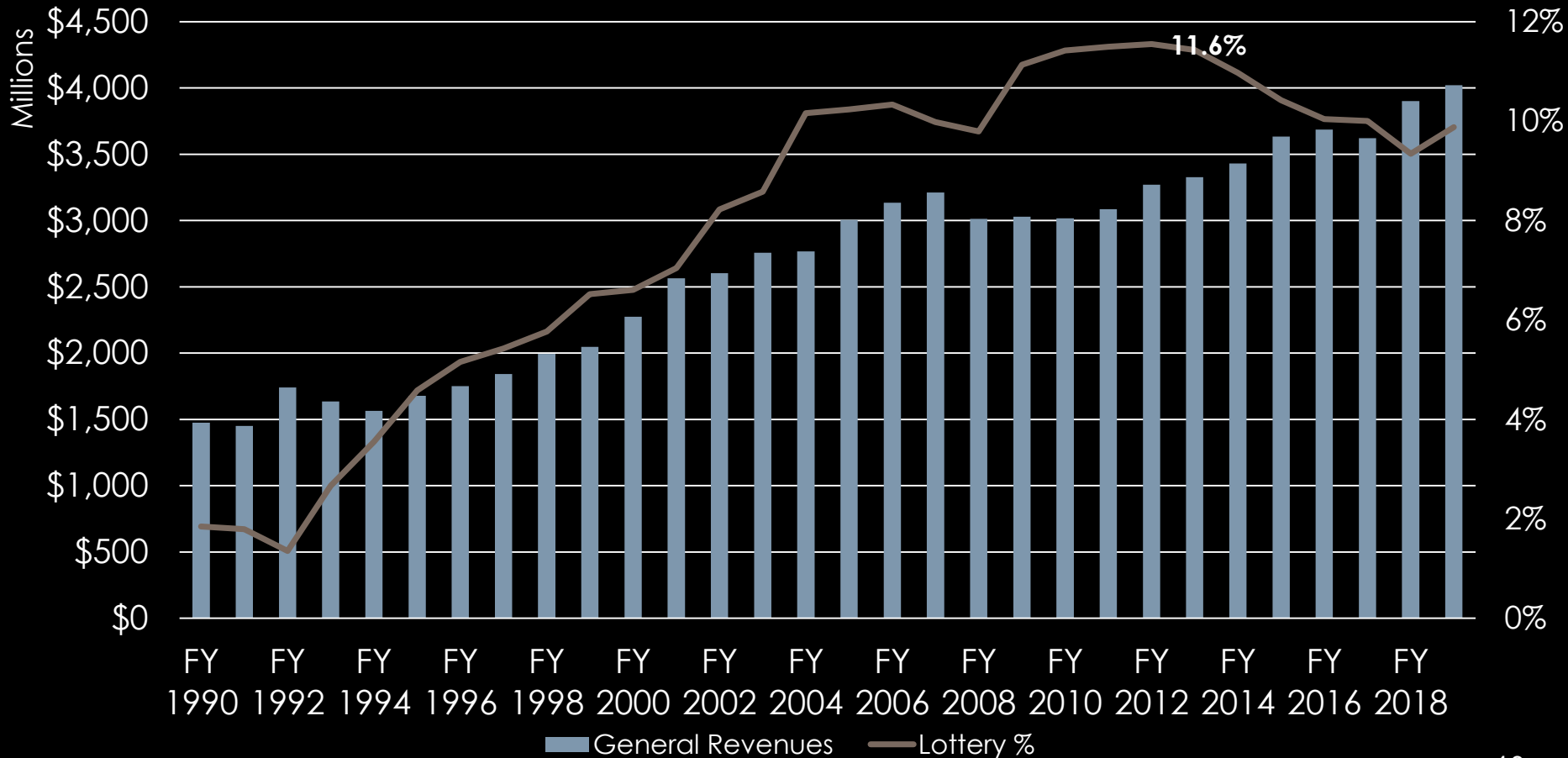
Background

Lottery Revenues FY 2000 – FY 2019



Background

**Lottery Revenues as % of General Revenues
FY 1990 – FY 2019**



Summary

- Background
- **Scope of Services**
 - **Traditional Lottery**
 - **Casino Operations**
 - **Economic Development**
 - **Other**
- Other Considerations

Scope: Traditional Lottery

- IGT responsible for technology and infrastructure, equipment and supplies used for sales and management of traditional lottery products
 - ~1,200 Retailers
 - Approx. \$260 million in sales

Products
Instant (scratch) Tickets
Numbers Games/Multi-state Games
Monitor Games: Keno, Bingo

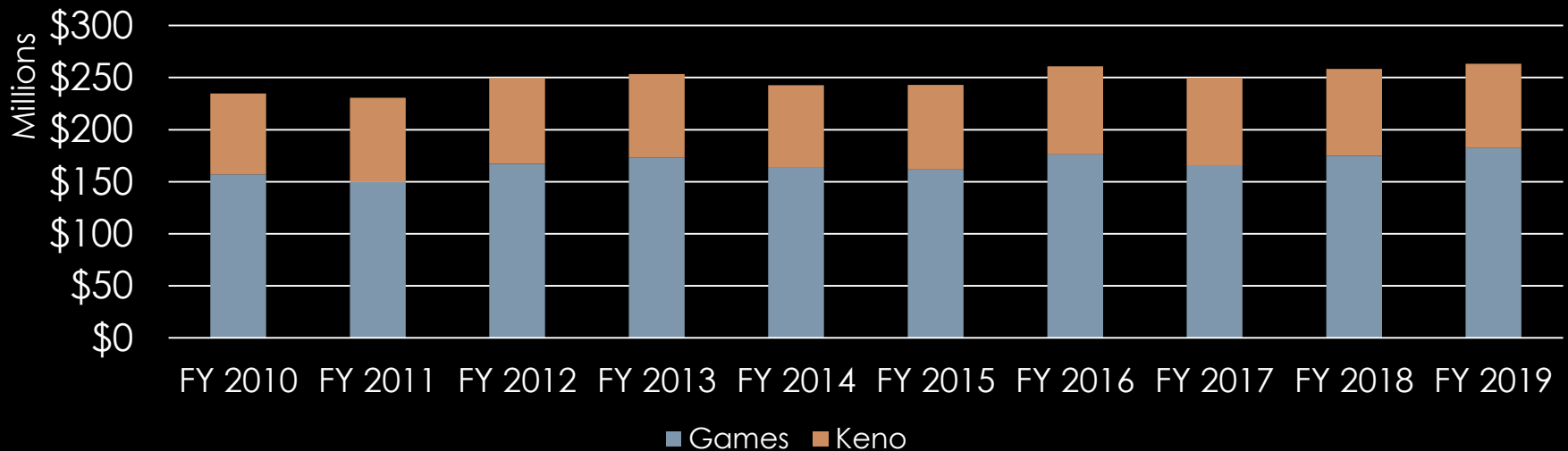
Scope: Traditional Lottery

- Vendor payments based on sales volume
 - Retailers receive 5% or 8% depending on game
 - IGT receives a percent based on total sales
 - Share reduced for sales over \$275 million
 - Sales have never reached that point
 - FY 2019 value approximately \$13 million

Sales Volume	Current	Proposed
Up to \$275M	5%	5%
\$275-\$400M	1%	4%
Over \$400M	5%	5%

Scope: Traditional Lottery

Lottery Sales



- New proposal calls for IGT to take over current sales force
 - 12 state employees
 - Estimated value \$1.3 million

Scope: Traditional Lottery

- Related Services – not in 2003 contract
 - iLottery
 - Full range of online lottery games offered within RI by October 1, 2021
 - Replacement by April 1, 2033
 - Limited offering assumed in FY 2020 budget
 - Instant ticket printing
 - Lock in pricing agreement reached in 2016
 - Add 36 new licensed instant ticket products over life of deal

Scope: Traditional Lottery

- 2003 maintenance/upgrade requirements delayed, modified, exchanged for other items
 - First system replacement due Jan. 1, 2007
 - Modified & delayed twice - done Oct. 14, 2007
 - Second replacement due Jan. 1, 2015
 - 2014 – delayed 4 years
 - 2017 – portion delayed up to one year and others delayed until no longer supported
 - 2018 – delayed obligation relieved with caveats

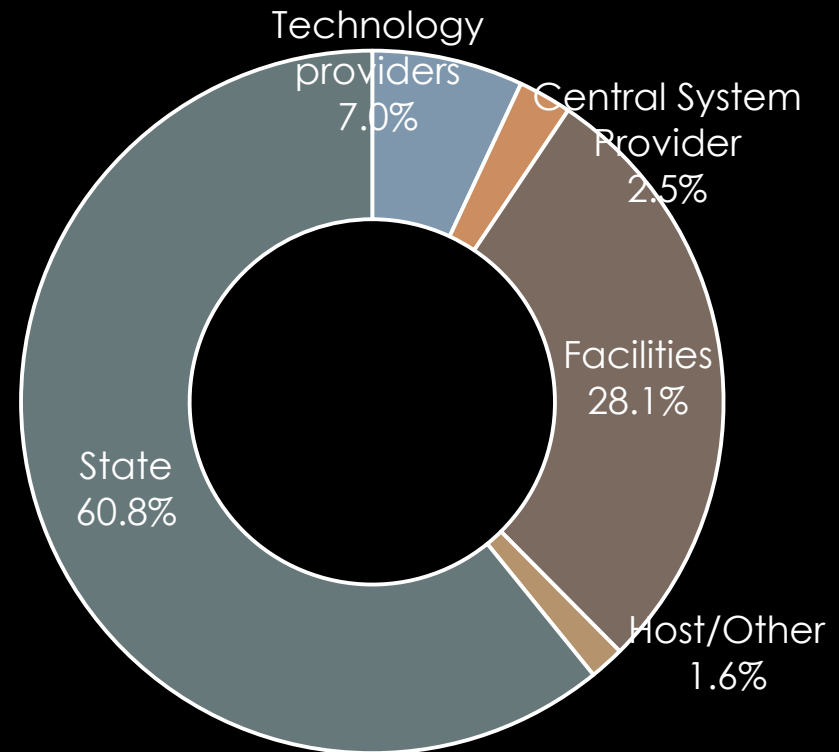
Scope: Traditional Lottery

- Maintenance requirements
 - Proposed legislation: “regularly update hardware and software”
 - Agreement in Principle:
 - Full replacement of internal control system by July 1, 2020
 - Full replacement of system by July 2031
 - More prescriptive provisions in agreement to ensure items kept up to date
 - Options for future expansions

Scope: Casino Operations

- Revenue earned through VLTs is split among many entities depending on their roles
- IGT has 2 roles related to VLTs

Share of NTI: FY 2019



Scope: Casino Operations

Two Distinct Roles

Central Communications System Provider

Technology (VLT machines) Provider

- IGT responsible for providing & maintaining a central communications system for VLTs
 - Transaction data for revenue splits and related needs
 - Servicing and maintaining all VLTs
- IGT also provides ~85% of all current VLTs

Scope: Casino Operations

- As central communications provider, IGT is paid a % of all net terminal income (NTI)
 - IGT receives a percent based on total sales
 - Share reduced for NTI over \$500 million
 - FY 2019 value \$12.7 million
 - No change from current law proposed

NTI Volume	Current/Proposed
Up to \$500M	2.5%
\$500M-\$1,000M	1%
Over \$1,000M	2.5%

Scope: Casino Operations

- VLT Machine providers are paid a % of their net terminal income (NTI)
 - 7% when daily NTI per VLT is \$325 or less
 - Share reduced to 1% for amounts over that
 - FY 2019 daily VLT per machine = \$277
 - FY 2019 payouts = \$36 million

Daily NTI per VLT	Current/Proposed
Up to \$325	7%
\$325 - \$500	1%
Over \$500	7%

Scope: Casino Operations

- Multiple vendors provide VLT machines for the two casinos
- Subject to annual efficiency review which could redistribute shares based on performance
 - 13-week measure of NTI % vs machine %
 - 50% of machines earning more than 50% of NTI is over 100% efficiency

Scope: Casino Operations

- Tool for the state to help maximize revenues and improve performance
 - Ratings below 97% mean a technology provider can lose machines up to 15%
 - Those over 100% can gain machines
 - Lottery has discretion
 - Removals without reassignment if space needed
 - Changes related to Tiverton opening

Scope: Casino Operations

- Prior years of VLTs by technology provider
 - Total paid to all providers in FY 2019 = \$36 million

Provider	FY 2015	FY 2016	FY 2017	FY 2018	FY 2019
Scientific Games	50	100	632	632	618
WMS	532	532	Merged with Bally/SG		
GTECH/IGT	2,841	4,528	4,482	4,473	4,370
IGT	2,007	See GTECH/IGT			
MM/Everi	205	205	205	205	195
Total VLTs	5,635	5,365	5,319	5,310	5,183
GTECH/IGT	50.4%	84.3%	84.2%	84.2%	84.3%

Scope: Casino Operations

- March 2019 efficiency review showed 93% efficiency of IGT machines
 - 84% of the machines but only 73% of the NTI
- August 2019 Lottery announcement
 - IGT to lose 360 or 8% of its machines to other vendors
- Revenues “lost” from underperforming machines unclear
 - Depends on assumptions about how other VLTs would perform & player preference

Scope: Casino Operations

- VLT performance addressed in proposal
 - 25% of current VLTs to be replaced in 2020
 - Minimum of 6% of all VLTs annually
 - Additional upgrades required on a minimum of 2% annually
 - Increased numbers of premium machines at no additional cost to facilities
 - Minimum standards for Lottery review of lowest performing machines

Scope: Casino Operations

- Current statute limiting the central system provider to 50% of VLTs set in 1992
 - 2003 Act enabling master contract effectively removed the limit by reference for the term of current contract
- 2019-H 6266 changes the limit to 85%
 - Has no similar exceptions to the limit
 - IGT could not get more than 85% even with better performance
- Thus 50% limit applies if competitively bid

Scope: Economic Development

- Current contract and proposed extensions contain requirements for minimum employment and investments

Requirement	Current	Proposed
Minimum Investment	\$100M	\$150M
Investment Timing	w/in 5 years	N/A
Minimum Jobs	1,000 FTE	1,100 FTE
Minimum Pay	150% of minimum wage (\$15.75/hr)	

Scope: Economic Development

- Minimum investments increased 50%
 - No requirement that it be reached within 5 years
 - Prior requirement included substantial, time sensitive capital project
 - Current requirement is over life of contract
 - System replacement and enhanced machine replacement requirements likely to satisfy spending thresholds

Scope: Economic Development

- Job requirements not met several times
 - 2014 Taxation Audits
 - Confirms compliance for 2010 & 2011
 - Missed targets for 2012 & 2013 but GTECH disputed methodology, agrees to penalty
 - Methodology agreement for 2014 and after
 - 2016 Taxation Audits
 - 2014 and 2015 targets not met
 - 2016 Contract Amendment
 - 2014-2017 requirements waived in exchange for certain services and products

Scope: Economic Development

- August report provided by IGT identified 1,007 jobs
 - Position title list
 - Salary averages by category
 - Noted 20 vacancies pending

Category	#	Avg. Pay
Corporate	104	\$109,164
Finance & Legal	167	\$148,020
Technology	292	\$120,166
North American Lottery Support	144	\$128,612
File Service & Call Center	300	\$47,875
Total	1,007	\$103,320

Scope: Economic Development

- Deal includes only job count and minimum pay for every job
 - Current complement and pay scales not specifically provided for within agreement
 - Value of current mix of jobs could be captured through additional metrics
 - Total payroll thresholds linked to growth measure
- New proposal also requires IGT to let RI compete for new jobs not in RI
 - When IGT is adding or moving 30+

Scope: Other

- Current contract and proposed extensions include upfront payment for right to be exclusive provider of services

Upfront Payment	Current	Proposed
Amount	\$12.5M	\$25M
Timing	Immediate	FY 2021/FY 2022 Before new term
Refundable if terminated?	Prorated	No
Qualifying Expense?	Yes	Yes

Scope: Other

- Other items not in original contract but in some cases added over time are addressed in new proposal
 - Long term agreement on enhanced web services/Website hosting
 - Item has been separately negotiated over time and used as tradeoff for other changes
 - Remote sports betting - exclusivity
 - 18 months after app launch Lottery may consider adding new providers if appropriate

Summary

- Background
- Scope of Services
- **Other Considerations**
 - **Comparisons**
 - **Economic Impact**

Comparisons

- Comparisons across states are difficult given lack of comparable data
 - Length & scope not found in other states
 - Rhode Island's direct role in running casinos is rare
- Joint request for analyses used to drive decisions yielded raw materials
 - Three summaries of other states' contracts
 - Copies of contracts and RFPs

Economic Impact

- Currently available studies show significant positive impact of jobs on state's economy
 - Appleseed & Tebaldi (IGT)
 - Are all elements considered?
 - What is value of possible trade-offs of lower cost?
 - Are the assumptions valid?
 - Job distribution and salary assumptions
 - Investment obligations

Other Considerations

- Issues to consider:
 - How are contract trade-offs scored and analyzed to ensure value maintained?
 - What lessons from past experience are reflected in the new proposal?
 - Industry and vendor changes
 - What would competitive process look like?
 - Timing?
 - Cost?
 - What are the tradeoffs?

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