

The background of the slide is a collage of US one-dollar bills, tilted at various angles. The bills are primarily blue and white, with the portrait of George Washington visible on several. The text "TAXPAYERS PROTECTION ALLIANCE" is overlaid on a dark blue rectangular box in the upper left corner.

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Taxpayers Lose With Rhode Island Lottery Contract

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About TPA

The Taxpayers Protection Alliance (TPA) is a rapid response taxpayer group dedicated to analyzing and researching the consequences of government intervention in the economy. TPA examines public policy proposals through a non-partisan focus, identifying how government waste and overreach impacts taxpayers and consumers regardless of the political party responsible.

TPA holds government officials in the United States, and around the world, accountable through editorials, statements, coalition letters, public interest comments, and radio and television interviews. TPA recognizes the importance of reaching out to concerned citizens through traditional and new media, and utilizes blogs, videos, and social media to connect with taxpayers and government officials.

While TPA regularly publishes exposés and criticisms of politicians of all political stripes, TPA also provides constructive criticism and reform proposals based on market principles and a federalist philosophy. TPA empowers taxpayers and consumers to make their opinions known to their elected and non-elected officials and embraces bold solutions to hold an ever-growing government in check.

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Introduction

Across the country, states are increasingly seeing the benefits of legalized commercial gambling. But, even in the 24 states that foster the \$260 billion casino gambling industry, disparate taxation systems, regulatory morass, and bidding procedures create significant uncertainty.¹ These problems are particularly pronounced in Rhode Island which lacks a transparent process for determining which companies produce, control, and maintain gaming machines. As a new lottery contract is debated and discussed, taxpayers have a significant stake in state officials choosing the right vendor. Following the status quo and not competitively bidding the new contract could mean billions of dollars of lost revenue.

In contrast to states such as Maryland, West Virginia, and New York, Rhode Island relies on no-bid contracting to determine the contractor(s) for state gaming services such as the state lottery. Casinos within the state are operated by the Rhode Island Lottery and management of video gambling (which generates approximately 80 percent of state gaming revenues) is outsourced to private companies. A May 2003 agreement with the state gave 50 percent control of gaming machines to International Game Technology (IGT). This agreement, originally supposed to last until 2023, may soon be significantly expanded with the administration of Gov. Gina Raimondo currently petitioning the Rhode Island General Assembly to grant IGT a 20-year contract extension in lieu of a competitive process with multiple proposals.²

Despite little chance of consideration by the state, other companies have submitted their own proposals for administering gaming machines. International lottery company Camelot Lottery Solutions, in partnership with casino owner Twin River, has released a public proposal to the state with claims that their terms will offer significant savings to Rhode Island taxpayers and allow the state sufficient flexibility to change agreement terms if state officials are unsatisfied.³ If Camelot's savings claims are true, Rhode Island is incurring significant costs by not establishing a competitive bidding process.

The Taxpayers Protection Alliance (TPA) has conducted an evaluation of the costs (as well as projected benefits) of IGT's and Camelot's proposal in an attempt to quantify the impact of different contract scenarios on taxpayers and the state of Rhode Island. In addition, TPA analyzes the potential consequences of Rhode Island pursuing a no-bid contract process for lottery services. While this analysis is comprehensive, there are additional factors to consider when comparing IGT's proposal with a more competitive approach. For instance, the state is documented to have overpaid IGT for lottery central system services, which this research brief does not address. Therefore, TPA considers its estimates to be conservative.

¹ American Gaming Association. "State of the States 2019."

² Sherman, Eli. "Raimondo defends \$1B IGT contract to House lawmakers." *WPRI*. September 24, 2019.

³ Twin River Worldwide Holdings, Inc. "Twin River Creates Partnership with Camelot Lottery Solutions to Offer Competing Lottery Proposal and Requests Opportunity to Bid." *PR Newswire*. September 18, 2019.

Overview of Rhode Island Lottery Operations

The state-owned Rhode Island Lottery maintains and controls gambling operations within state, which have steadily expanded since Rhode Island legalized the use of video lottery terminals (VLTs) at state casinos in 1992 in response to the opening of Foxwoods Casino in Connecticut. Within a year of legalizing VLTs, more than 1,000 terminals were operational. But, because of legal restrictions and a prohibition on reel type video slot machines, revenue for the first year remained less than \$20 million.⁴ This was followed by a hostile political environment for casino operations, and in 1994, an amendment to the state constitution was ratified precluding the expansion of gambling in-state without majority approval in a state referendum.⁵ Regardless of this backlash, revenues on existing operations increased significantly. In an analysis of gambling revenue across the US from FY 1998 through 2006, Nelson A. Rockefeller Institute of Government researchers found: “West Virginia and Rhode Island experienced the largest increases in dependence on gambling revenue over the period [as a percentage of own-source revenue], at 6.4 and 3.3 percentage points, respectively.”⁶ Through increased gaming operation productivity and the introduction of table games in casinos in 2012 to complement gaming machines, business and revenue increased significantly. In 2018, for example, commercial revenue generated from the Twin River Casino Hotel and the Tiverton Casino totaled \$481.4 million.⁷

According to data provided by the American Gaming Association, “Rhode Island’s two commercial casinos retain roughly 26 percent to 28.85 percent of their revenue from electronic gaming devices, depending on each facility’s operating contract and state regulation...The state’s overall take of electronic gaming device revenue, after administrative and technology expenses are deducted, is about 60 percent.”⁸

As a result, the state collected more than \$320 million in tax revenues from casinos in 2018. This is a significant sum compared to other states. A 2016 study by the Nelson A. Rockefeller Institute of Government found that state gambling revenue in Rhode Island totals more than \$400 per adult resident, compared to a nationwide average of \$113.⁹

Gambling revenue is the third-largest source of income for the Rhode Island government. Despite this significant revenue intake from gambling, the state incurs unnecessary costs in administering VLTs. Machine operations are contracted out to private companies such as IGT, which charge the state government fees for operational expenses.

⁴ Christiansen Capital Advisors, LLC. “Rhode Island Gaming and State Revenue Forecast.” October 30, 2015.

⁵ Conley, Patrick T., and Robert G. Flanders. *The Rhode Island State Constitution: a Reference Guide*. Vol. 44. Greenwood Publishing Group, 2007.

⁶ Dadayan, Lucy, Nino Giguashvili, and Robert B. Ward. “From a Bonanza to a Blue Chip?: Gambling Revenue to the States.” *The Nelson A. Rockefeller Institute of Government*. 2008.

⁷ American Gaming Association. “State of the States 2019.”

⁸ Ibid.

⁹ Dadayan, Lucy. “State Revenues from Gambling.” *The Nelson A. Rockefeller Institute of Government*. April 2016.

As **Table 1** shows, fees for Rhode Island taxpayers are significantly higher than in other states.

Table 1. Annual VLT Central System Fees, Rhode Island and Comparable States (\$ millions)¹⁰

State	VLT Central System Fees
West Virginia	\$ 0.4
Oregon	\$2.1
Massachusetts	\$ 2.3
Delaware	\$ 3.5
Pennsylvania	\$ 3.7
Rhode Island	\$ 12.0
Similar States Average	\$ 2.4

Rhode Island pays a significant premium to private vendors for managing state-owned VLTs, which is likely due to the state's tendency toward no-bid contracts for gambling operations. Unlike Rhode Island, the listed comparable states engaged in competitive bidding, resulting in rival companies making their case to states and taxpayers that their services are cost-effective.¹¹

In contrast, Rhode Island has repeatedly awarded no-bid contracts for lottery and video gambling operations. While other companies have released alternative proposals to IGT's preferred terms, there is little indication that the Raimondo administration will consider rival bids. Most significantly, Camelot Lottery Solutions has released a proposal to the public detailing a more cost-effective alternative to the proposed IGT 20-year contract extension.¹² **Table 2** compares both proposals.

Table 2. IGT and Camelot Proposals at a Glance^{13 14}

	Camelot/ Twin River	IGT
% Control over Slot Machines	50%	85%
Length of Contract	12 years	20 years
Estimated Jobs Created	1,100	1,110
Contract Linked to Job Creation?	YES	NO
Annual Cost to Taxpayers	\$40 million	\$55 million
Cost to Taxpayers over Contract Lifetime	\$480 million	\$1.1 billion

¹⁰ LaFleur's World Lottery Almanac, Lottery annual reports, state documents.

¹¹ See, for example: Murphy, Jan. "\$800 million jackpot: Companies battle for Pa. lottery contract." *The Patriot-News*. July 30, 2018.

¹² Twin River Worldwide Holdings, Inc. "Twin River Creates Partnership with Camelot Lottery Solutions to Offer Competing Lottery Proposal And Requests Opportunity To Bid." *PR Newswire*. September 18, 2019.

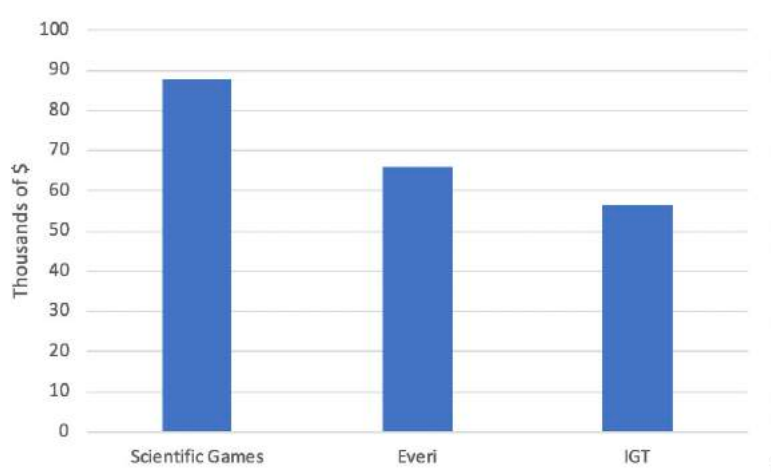
¹³ Ibid.

¹⁴ Sherman, Eli. "Raimondo defends \$1B IGT contract to House lawmakers." *WPRI*. September 24, 2019.

As can be seen in Table 2, Camelot’s proposed operation fees are significantly lower than IGT’s, resulting in significant cumulative savings to the taxpayer of \$180 million over the 12-year length of Camelot’s proposal. IGT has proposed providing and managing 85 percent of the gambling machines in Rhode Island’s casinos, effectively denying competitors the ability to control enough machines to demonstrate cost-effectiveness. Camelot’s proposal reflects a more competitive approach and allows the state to renegotiate or choose a rival operator in 12 years.

Cost savings from lower state fees and greater contract flexibility, however, are just one component of likely wider overall savings for Rhode Island taxpayers. IGT machines tend to produce less overall revenue than current rival operators, resulting in the forgoing of significant amounts of tax revenue. **Figure 1** records total fiscal year (FY) 2019 tax revenue generated per Rhode Island gaming machine.

Figure 1. Total FY 2019 Tax Revenue Generated per RI Machine, By Company ¹⁵



On average, IGT’s competitors’ machines each generate \$77,000 in tax revenue, compared to \$56,400 for each of IGT’s machines. For this analysis, TPA assumes that IGT would provide and maintain 85 percent of VLTs in the state if their contract was extended. In contrast, IGT would retain control of 50 percent of VLTs if the state came to an agreement with Camelot or another provider. According to the American Gaming Association, there are currently 5,180 machines in commercial casinos in Rhode Island.¹⁶ **Table 3** projects tax revenue for the first year under competing proposal scenarios.

Table 3. Difference in Tax Revenue for Competing Proposals, Year 1

	Scenario 1: IGT Contract Extension	Scenario 2: Camelot Proposal Accepted
IGT-Controlled Machines	4,400	2,590
Competitor-Controlled Machines	780	2,590
Tax Revenue Generated	\$308.2 million	\$345.5 million

Table 3 demonstrates significant differences in tax revenue under competing proposals in just the first year. In year 1, the Camelot proposal would generate over \$37 million more in tax revenue than the IGT proposal. Over the 12-year life of the Camelot proposal, this revenue gap would widen to \$448 million.

¹⁵ RI Lottery Video NTI reports.
¹⁶ American Gaming Association. “State of the States 2019.”

Conclusion and Overall Savings

Under the status-quo, Rhode Island will continue to rely on no-bid contracting and IGT will likely get their contract extended by 20 years. This approach, favored by the Raimondo administration and legislative allies, would result in IGT providing and maintaining 85 percent of gaming machines located in state-operated casinos. An IGT contract extension, however, would entail significantly-higher annual operating fees and result in foregone state tax revenue relative to alternative, more competitive proposals. **Table 4** totals annual and cumulative differences in state expenditure and tax revenue between available proposals.

Table 4. Annual and Cumulative Difference in Net Revenue for Competing Scenarios (\$ Millions)

	Scenario 1: IGT Contract Extension	Scenario 2: Camelot Proposal Accepted
Tax Revenue Generated	\$308.2	\$345.5
Direct Costs to Taxpayers	\$55.0	\$40.0
Net Revenue, Year 1	\$253.2	\$305.5
Net Revenue, Year 12	\$3,038.4	\$3,666.0
Net Revenue, Year 20	\$5,064.0	\$6,110.0

By the end of IGT's proposed contract life, net revenue would be more than \$1 billion less than under Camelot's proposal. The key driver of this significant gap is the revenue potential of IGT machines versus machines produced and operated by rivals, though IGT's user fees are also a significant factor behind the revenue discrepancy.

It is tempting to conclude from this analysis that one company is systematically better or more efficient than another. In fact, different companies can produce a wide range of efficiency and revenue outcomes under different conditions. For instance, IGT fees for VLT systems are 3 to 6 times lower in Pennsylvania and Oregon than in Rhode Island, due to the former states having a more competitive bidding process than Rhode Island. This suggests that moving to a competitive bidding system is more important to long-run growth and tax collections than endorsing only one proposal.

Rhode Island can, however, realize significant savings by considering multiple bids, including Camelot's proposal. Embracing competitive bidding has the potential to save billions of dollars each decade by openly and transparently considering all proposals rather than just one.