



December 15, 2006

*Via Facsimile Transmission and U. S. mail*

National Indian Gaming Commission  
1441 L Street, NW, Suite 9100  
Washington, D.C. 20005  
Attn: Penny Coleman, Acting General Counsel

***Re: IGT Comments on Economic Impact Studies***

Dear Ms. Coleman:

This letter comments on the Economic Impact Study commissioned by the National Indian Gaming Commission ("NIGC") released on November 6, 2006. IGT previously submitted extensive comments through correspondence to the NIGC regarding the Commission's efforts to establish technical standards, definitions, and classification regulations for Class II gaming.

**Study comparison**

We have completed a comparative analysis of "The Potential Impact of the NIGC's Proposed Class II Game Specification Regulations on Class II Tribal Gaming", a study conducted by The Rose Institute of State and Local Government at Claremont McKenna College (Submitted to NIGC by IGT on November 14, 2006) and "The Potential Economic Impact of Proposed Changes to Class II Gaming Regulations" by Alan Meister, Ph.D. of the Analysis Group, Inc. Each study examines the impact of the implementation of the proposed Class II game classification standards on tribal Class II gaming.

Both studies considered the changes to play that would come from the proposed regulations and both studies reached similar conclusions as to the potential impact of the proposed regulations on tribal gaming revenues from the play of Class II games with technologic aids. Further, a simulation analysis conducted for NIGC and referenced in the Meister study confirms game play assumptions in the two studies. Each study, independently and using different methods of analysis, concluded that implementation of the proposed Class II game classification standards on tribal Class II gaming will result in reduction of tribal revenue from tribal Class II gaming of over one billion dollars per year.

Both studies also acknowledged additional losses that would occur in tribal employment, non-gaming revenue, and the possible demise of smaller tribal Class II operations that presently benefit poorer tribes whose Class II revenues comprise a greater share of total tribal revenues

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than the norm. Finally, each study acknowledged the damage that will occur to tribes such as those in Florida who would see their leverage in Class III negotiations severely damaged by the implementation of the proposed regulations.

### **Secondary analysis**

Both the Rose Institute study and the Meister study examined the potential loss of revenue from Class II gaming given the implementation of the proposed regulations. However, in the core area of tribal gaming revenue, the Meister study included a secondary analysis of lost revenues that might be recouped by tribes switching to Class III devices where Meister believes that option is available.

We submit that the tribal response to the loss of revenue from these regulations is a separate issue from the question "What impact will these proposed regulations have on Class II tribal gaming?" Further, we submit that, even if one were to consider avenues for relief from the damage caused by the proposed regulations, the relief suggested in the Meister study is not entirely viable.

Meister concludes that, net of games that may be replaced by Class III games; tribal revenue loss from implementation of the proposed regulations will be reduced from \$1.48 billion to \$142.7 million. This reduction of \$1.34 billion is suspect on several counts: The reduction in the amount of loss assumes tribes in Oklahoma, Florida, California, and elsewhere can switch to compacted, Class III games; the reduction estimate does not account for the revenue-sharing expense that will occur as a result of tribal conversion from Class II to Class III games; and the reduction estimate for tribal revenue loss does not account for the capital expense of replacing Class II gaming systems with Class III machines nor for the capital expense of converting the remaining games to be compliant with new regulations.

#### *Tribal ability to compact for Class III gaming –*

The Meister study assumes that tribal revenue losses from implementation of the proposed regulations will be mitigated by tribal use of Class III games. He suggests that tribes in Arizona, California (except for the Lytton Band's gaming facility), Florida, Oklahoma, Oregon, and Wyoming can simply switch to Class III games. However, that assumption is not supported in key jurisdictions.

In Florida, which accounts for 8,598 games or 18.9% of the reduction in loss, the state and tribes have not been able to negotiate Class III gaming compacts. Despite authorization of slot machines in the state, prolonged negotiations between the state and tribes eventually broke off with no agreement. A proposal to put Class III Procedures in place will face a legal challenge from the state.

In California, whose Class II games (less those at Lytton) in 2005 accounted for approximately 1,600 or 3.5% of the reduction in loss (today California has nearly twice that number less Lytton games), ratification of compact amendments has stalled in the legislature and tribes are operating Class II games in addition to their Class III games precisely because they have not been able to amend their compacts and increase the number of compacted games they operate.

In Oklahoma, which accounts for 28,601 games, or 63% of the loss, tribes do have the option to compact for Class III games simply by choosing to do so.

Inexplicably, while the Meister study assumes tribes have the option to compact or amend compacts in Florida or California where there are no compacts or where compact ratification is stalled, he assumes tribes cannot replace Class II games with Class III games in Minnesota, Montana, New York, South Dakota, Washington, and Wisconsin – states that have entered into compacts (although they pose many of the same challenges to compact amendment that presently exist in California).

The current inability of tribes to compact for more Class III games in California and Florida would reduce the \$1.34 billion reduction in gaming revenue loss by at least 22.4% or \$300 million.

*Revenue sharing expense –*

The Meister study's conclusion that tribal revenue loss from implementation of the proposed regulations can be reduced by tribes switching to compacted games does not account for the revenue sharing expense that tribes will incur. Meister estimates that Oklahoma tribes will pay from \$49.6 million to \$74.5 million per year in revenue-sharing to the state. However, that additional expense is not reflected in his \$142.7 million revenue loss figure.

In California tribes have recently negotiated compacts and compact amendments that include revenue sharing as high as 25% of net win on certain portions of tribal gaming revenue. As the Class II game systems now in use in California are typically in place to serve the top tier of market demand in peak periods it is reasonable to assume that compacted Class III machines which replace Class II games would be subject to the highest levels of revenue sharing.

In Florida, where no state-tribal gaming compacts have been negotiated, it is impossible to estimate what the revenue-sharing burden would be on compacted Class III machines in the event compacts are negotiated. However a less-viable Class II game will certainly weaken the negotiating position of Florida's tribes.

Revenue sharing would diminish the reduction in gaming revenue loss by the \$49.6 million to \$74.5 million per year in revenue-sharing that Oklahoma tribes would need to pay to the state for 28,601 compacted games, or, an average of \$62.05 million.

If tribes could get compacts or compact amendments on the more than 10,000 Class II games that would need to be replaced in Florida and California it is not known what share of revenues would need to be paid to the states. 10,000 machines with revenue sharing obligations similar to Oklahoma's would result in further tribal losses of between \$17.36 million and \$26 million. At those rates, for Oklahoma, California, and Florida, the \$1.34 billion reduction in gaming revenue loss would be reduced by \$67 million (5%) to \$100.5 million (7.5%).

*Capital expense –*

The manufacturers group involved in analyzing the proposed regulations has been working to estimate the expense to provide a product to fit the proposed regulations. It is estimated that it would cost the various manufacturers involved in Class II over a billion dollars to replace or convert existing Class II games to compliant games under the proposed regulations. Manufacturers would need to be confident that tribal customers would be willing to bear this cost before they could proceed with the requisite capital investment.

The Meister study suggests that tribes can reduce the revenue loss they will incur with the implementation of the proposed regulations by replacing Class II games with compacted Class III machines in California, Florida, and Oklahoma. However, the Meister study doesn't factor the cost of such replacement into its calculation of tribal revenue loss. Whether the replacement Class III machines were provided to tribes on a lease or sale basis, tribes would incur a substantial additional capital expense that would not be necessary but for their virtually forced conversion to Class III games. That additional capital expense for Class III machines or for new, compliant Class II games does not include the unrealized use of existing Class II equipment and the balance of debt or the unrealized earnings on same.

Thus, whether or not tribes convert to Class III machines to the extent the Meister study suggests, tribes will face a substantial capital or lease expense as a result of these proposed regulations.

**Conclusion**

We believe it is compelling two independent studies of the potential impact of the proposed Class II regulations each concluded that revenue loss to tribes would be greater than one billion dollars per year.

We do not agree that an evaluation of revenue loss from the proposed regulations should be offset to include additional revenue earned by tribes through implementation of Class III gaming.

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And, while we do not agree with the inclusion of Class III revenues as an offset, we submit that any such offset should not include states where no compacts currently exist nor states where the compact and compact amendment ratification process is currently stalled and that any such offset must be net of revenue-sharing expense and net of requisite capital expense. In that case, the \$1.34 billion that the Meister study suggests tribes could recoup from their Class II losses would need to be reduced by the \$300 million he suggests could be saved in California and Florida, by the \$62.05 million in annual revenue-sharing expense that would be borne by Oklahoma tribes, and by the hundreds of millions of dollars required to convert Oklahoma game systems to Class III machines and to convert all other Class II games to Class II games compliant with the proposed regulations.

Thus, even if tribes converted to Class III machines where they were able, the offsetting revenues, net of additional revenue-sharing and capital expense would be much less than the \$1.34 billion suggested by the Meister study. And such conversions would come at the expense of significant erosion in tribal leverage to negotiate Class III compacts and the possible demise of smaller tribal Class II operations that presently benefit poorer tribes whose Class II revenues comprise a greater share of total tribal revenues.

We submit that the key result of these studies is their agreement that the proposed Class II classification standards will result in annual tribal Class II revenue losses of over one billion dollars. We further submit that the resulting revenue loss cannot be recovered with other forms of gaming so easily nor so completely as the Meister study suggests.

I hope this information is helpful to the Commission. Please feel free to contact me at (702) 896-8597 if you have any questions or would like additional information. Thank you in advance for your consideration.

Sincerely,



Gayle Bauer

Regulatory Compliance Manager

c: Michelle Chatigny  
Knut Knudson  
Judith A. Shapiro, Esq.