

2010

SUMMARY REPORT:

**COMPARING THE ECONOMIC COMPETITIVE ADVANTAGES OF
INDIAN RUN CASINOS LOCATED ON SOVEREIGN LANDS IN
WESTERN NEW YORK OVER OTHER HOSPITALITY OPERATIONS**

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ABSTRACT:

For the 9 months ending June 30, 2010, the casinos operated by the Seneca Gaming Corporation (SGC) returned over \$42,000,000 (out of \$392,949,000 in customer gambling losses) to gamblers. These points are redeemable only at their casinos for food, beverage, hotel rooms, entertainment and retail products. The goal of this program is to keep the gambler coming back to the casino, but it also serves to effectively discourage them from patronizing local hotels, restaurants, bars and entertainment venues where they would have to actually pay for the products and support the local economy.

But these products are not really “free” – they are simply a small portion of gambling losses returned to the gambler. The “hold” at the casinos as reported in the latest security and exchange commission (SEC) filing was 7.8%, therefore for every dollar gambled, the average return to the gambler was \$.92 with the casino keeping \$.08. The \$42,000,000+ was a small portion of the \$.08 returned to the gambler in the form of “player points” redeemable only within the casino.

Through utilizing over \$42,000,000 in “loss leaders” as well as through strategic competitive advantages based upon being a sovereign nation and therefore operating under a different set of rules, regulations and laws as compared to all other hospitality entities that they compete with, they pose a formidable threat to any and all other hospitality operations in WNY. The continued viability of that vibrant industry as an economic generator would be at stake if the Buffalo Creek Casino was ever completed.

The Seneca Gaming Corporation has constantly attempted to convince the citizens of WNY that their casinos will provide long-term economic benefits to the area. The local “mainstream” media has, with few exceptions, repeatedly quoted the statistics that the SGC’s public relations people have provided them. The mainstream media has rarely if ever done an independent analysis of the numbers or sought answers to some of the more disturbing statistics.

The current legal challenges will eventually work their way through the courts and most interested citizens have staked out their own personal opinions on the attendant moral and social issues. But in these hard economic times, what is essential for every concerned citizen to become aware of is the additional long- term economic damage that the current gambling facility and the proposed casino will bring to the Buffalo area.

What the public hears from the media about the supposed economic impact of the casino is a series of very large numbers.....\$200 million in revenue, 1,400 new jobs, etc. What we rarely hear about is the devastating negative economic impact that research shows occurs when a tax exempt casino is placed on sovereign land within an urban setting. The citizens of WNY need a true accounting of the millions of dollars from the operation of a casino that would leave the area and flow to Albany. They also need to be told that this proposed casino will actually cause a net loss of jobs which will continue to hemorrhage out of WNY each year that the casino would be in operation. Perhaps most importantly the SGC’s own financial numbers as presented in their Security and Exchange Commission filings clearly indicate that if a full-service casino is constructed anywhere within the City of Buffalo, the impact on the lodging, food

and beverage and entertainment industries will be devastating – causing the few first class hotels in the city to lower rates and expenses (with a concomitant lowering of quality) in order to compete. This scarcity of first class hotel rooms could jeopardize the ability of the Buffalo/Niagara CVB to book conventions and trade shows, as well as cause many restaurants and bars and entertainment venues to fall upon hard times.

There exists hard data that should make it clear to our citizens and decision makers that not only won't the casino deliver on its inflated claims, but it would actually serve as a huge money sucking vacuum, redirecting hundreds of millions of dollars from local businesses and putting far more people out of work than it can ever hope to employ in the casino.

Specifically:

- **The temporary casino in Buffalo has, to date, only generated approximately \$700,000 for the city (\$200 million worth of payments to New York State are currently in legal limbo).** To put that in perspective this money would fund the daily operation of the Buffalo police department for 3 days or the fire department for 4 days. \$700,000 is 6 one-hundredths of 1% of the city's budget. – Hardly a windfall source of revenue. Source – City of Buffalo adopted budget 2008-09
- **Research shows that for every 3 video slot machines in any casino, that area will, within the second year of operation, lose 2 jobs in the local economy.** The proposed casino in Buffalo would have between 1900 and 2200 slot machines, so if the project is built, we can expect to lose between 1200 to 1400 jobs each year. The larger the casino, the more slot machines it contains, the greater the job loss to the local economy. Source: Professor John Kindt- U of Illinois, 2001 – Analysis, Professor Steve Siegel – Niagara U., 2008.

Why? Because every 3 SGC video slot machines, on an average year, sucks between \$210,000 to \$250,000 in discretionary spending out of our economy. Therefore the revenue from any 3 slot machines will displace over \$200,000 that could have been spent at other area businesses. Assume that each dollar lost in a slot would have had a \$2 impact on the economy due to being spent more than once (multiplier effect) and you have approximately \$400,000 that isn't being spent at the local dry cleaners or the butcher shop or the bowling alley. Business owners respond to reduced volume by laying people off in order to reduce costs. Thusly the more money that goes into the slots, the less that goes into local small businesses.

The larger the casino, the more devastating the impact on the local unemployment situation. At the current projected size for the proposed casino, within 2 years the local economy will lose far more jobs than the SGC claims it will create and the area will continue to lose more jobs each subsequent year.

- **The City of Buffalo estimates that if the casino is built the payback from Albany to Buffalo would be between \$ 5-7 million per year.** Given the huge impact that the current recession is having on the gaming industry we can assume that the \$5 million figure is closer to the

truth. To put this in perspective we can again look at the City of Buffalo's 2008-09 adopted budget. In this budget the city projects that revenue from "Parking Enforcement" will be \$7.75 million dollars. *So the casino, with all its attendant social and economic costs, will bring to the city only 65% of what writing parking tickets will bring in.*

- **Albany currently gets 25% of the slot revenues and passes on only 25% of that to the city.** So this means that for every \$1 that a local gambler loses in a slot machine, the Senecas and Albany keep 93.75 cents and the City keeps 6.25 cents. Yet we are the host community dealing with all the attendant costs of the casino – social and otherwise. A terrible financial arrangement for the city.
- **For the 9 months ending on June 30, 2010, \$4,597,842 (BILLION) dollars in "slot handle" passed through the slot machines at the existing SGC casinos.** Projecting "handle" for any one year and it will be approximately **6 BILLION DOLLARS**. Can we really afford to have economic activity of this magnitude concentrated in an entity that contributes so little to improving the social and economic fabric of the community in which we all live? 6 Billion dollars is spent yearly on a product which costs little to create and therefore returns little economic value to the community, but much in the way of social problems.
- **For the 9 month period ending June 30, 2010 the SGC operated all their non-gambling services which include food, beverage, retail sales, entertainment and hotels at a loss of over \$50 million** (see chart). In other words they give it away free.

#1 - Estimate of operating loss from all sources other than gaming: (Food, Beverage, Lodging, Entertainment, Retail)

Operating loss from all sources other than gaming: 9 month ending June 30, 2010

Revenues

Food and beverage	41,337,000
Lodging	17,885,000
Retail, entertainment and other	16,800,000
Gross Revenue	<u>76,022,000</u>
Less: Promotional allowances	<u>-42,743,000</u>
Net revenues	\$ 33,279,000

Minus direct expenses from all sources other than gaming:

Expenses (Direct)

Food and beverage	31,824,000
Lodging	8,747,000
Retail, entertainment and other	10,711,000
Direct - F&B, Lodging, R&E	51,282,000

LOSS from all sources exclusive of gaming	(33,279,000 - 51,282,000)	-18,003,000
*Assign 20% of indirect expenses (\$171,555,000):		-34311000
Estimate of loss from all non-gaming operations:		\$ (52,314,000)

* conservative estimate

- **Promotional Allowances (Player Points Redemption)**

Specifically: (from SEC filing)

80% of guest room revenue was not realized - given away complimentary.

52% of food and beverage revenue was not realized - given away complimentary

73% of entertainment tickets issued and retail merchandise distributed was given away free

The following chart quantifies the promotional allowances provided by each category for the 9 month period ending June 30, 2010 which totaled in excess of \$42,000,000.

Promotional Allowances

SGC operates a complimentary program in which food and beverage, retail, entertainment, and other services are provided to patrons based on points earned through the Seneca Link Player's Card. The retail value of these complimentary items is included in gross revenues and then deducted as promotional allowances to arrive at net revenues. The retail value of providing such promotional allowances was included in revenues as follows:

	Nine Months Ended June 30, 2010
	(Dollars in Thousands)
Food and beverage	21,307,000
Lodging	14,317,000
Retail, entertainment and other	7,119,000
Total	\$ 42,743,000

The impact that this will have if the casino is ever opened in Buffalo would be to drive many hotels, restaurants and entertainment venues out of business because it is impossible to compete with an entity that gives away the product for free. There is no known business strategy for competing in this type of competitive environment.

The casino not only diverts large sums of discretionary spending away from other local businesses and into the casino (\$4.5 Billion), but to compound the "financial hit" to the local hospitality industry the casino then gives the gambler back promotional points which can only be redeemed in the casino - and were - to the tune of \$42,743,000 worth of food, beverage, entertainment and retail sales.

- The chart below provides 3 common measures for gauging the operational success of any hotel. Column #1 comes from Smith Travel Research and provides data for hotels in WNY for the period of March 30, 2009 to March 30, 2010. It represents performance data for all hotels considered in the "Upscale-Upscale segment of the WNY market (such as Hyatt, Adams Mark, Marriott etc.). Column #2 and #3 represent performance data from the 2 SGC

hotels (Niagara Falls and Salamanca). Column #2 is unadjusted for the 80% of rooms given away complimentary (in other words, includes the revenue that they would have received but didn't). Column #3 adjusts for the \$17,885,000 of room revenue not "realized" or not received and represents true cash flow. *In analyzing column #3 we can quickly conclude that any hotel (regardless of what sector of the lodging market) running the numbers present in column #3 would be out of business in a matter of months.*

	WNY HOTELS	CASINO HOTELS	CASINO HOTELS
		"UNREALIZED"	"REALIZED"
	Column1	Column2	Column3
Percentage of Occupancy	75.80%	92.20%	* 18.44%
Average Daily Rate	\$101.30	\$90.58	\$16.04
Revenue Per Available Room	\$76.76	\$83.48	\$33.50

*paid

- The chart below clearly shows why restaurants located within a casino and subsidized by hundreds of millions of dollars of gaming revenues can easily undersell all restaurants in the area and effectively put them out of business.** You can see from these figures taken from the SGC's 10K SEC report that *that every time their restaurants provide a meal they are losing somewhere in the neighborhood of \$1.50 to \$2.00 per meal.* Imagine a restaurant giving away almost 3 meals per minute, 24 hours per day, 7 days a week and losing \$1.76 on each meal. **Yet the entity it is located within would report net income for 9 months of \$83,607,000** (net income for the SGC's three casinos for the 9 month period ending June 30, 2010).

#3 - Analysis of Average Food and Beverage Check - Casinos: 270 day period

Given:

Average Check =	\$ 14.70
Complimentary F&B =	\$ 15,949,000
Days in period =	270
F&B revenue complimentary =	52%
F&B revenue realized =	48%
Estimate of "Prime Costs" (Product + labor) for average restaurant	60%

Analysis "A": Loss per meal provided

"Realized" revenue per average check: \$14.70 x 48% =	\$ 7.06 Revenue
Apply 60% prime costs to "unrealized" average check = \$14.70 x 60% =	\$ (8.82) Prime variable expense
	\$ (1.76) Estimate of casino loss per meal provided

Analysis "B": Number of complimentary meals provided (270 day period)

Complimentary Product divided by average check =	1,084,966 Meals
Complimentary meal per day =	4,018 Meals per day
Complimentary meals per hour =	167
Complimentary meals per minute =	2.79

Analogies: (for the 9 month period ending 6/30/2010)

- The SGC gave away an average of 653 hotel rooms per night, every night. This is more rooms given away per night than the total number of rooms that the Adams Mark and the Buffalo Hyatt SELLS on an average night for 365 successive days. A large hotel, as planned for the Buffalo Creek site, would drain off a considerable amount of business from local upscale hotels. Given that hotels need to sell an average of approximately 60% of their rooms each night to break-even, even a small perturbation in the competitive market structure can turn the property into a money losing operation.
- If we assume that the average expenditure on F&B by each person attending a Sabre game is *\$14 per game, the Sabres would have to give away \$14 worth of F&B to each of 18,690 fans (sellout) for 2 entire seasons in order to provide the same amount of free food and beverage that the casinos provided in the 9 month period.
- The \$7,119,000 in “promotional entertainment” is equivalent to the Sabres giving away 4,823 free tickets per game, each game, for a 41 game home season (average ticket price = \$36 for 2009-10 season, Forbes Magazine).
- The highest grossing restaurant in the downtown corridor grosses ½ the F&B revenue that the SGC gives away in promotional F&B.
*estimate

Comparison of legal requirement for SGC casinos vs. all other hospitality operations in WNY:

LEGAL REQUIREMENTS	REQUIRED OF NON-CASINO ENTITIES?	+REQUIRED OF SGC CASINOS?
PAY PROPERTY TAXES	YES	NO
COLLECT SALES TAX	YES	NO
COLLECT BED TAX	YES	NO
APPLY FOR AND PAY FOR LICENSES	YES	NO*
ABIDE BY ANTI-TRUST LAWS	YES	NO
SUBMIT TO HEALTH INSPECTIONS	YES	NO
LEGAL LIABILITY	YES	LIMITED
PUNITIVE DAMAGES	YES	NO
SMOKING BAN	YES	NO
LIMITED HOURS – LIQUOR SALES	YES	NO
COMPLY WITH LABOR LAWS	YES	NO

**CASINO MUST PROCURE LIQUOR LICENSE – BUT ONLY SO LIQUOR DISTRIBUTORS CAN DELIVER TO THEM*

+CASINOS MAY COMPLY WITH ALL OR NONE OF THESE LAWS/REQUIREMENTS, BUT IT IS TOTALLY OPTIONAL AND NOT LEGALLY REQUIRED AS THEY ARE A SOVEREIGN NATION.

Summary:

In my 34 years researching and teaching in the area of strategic management for the hospitality industry, I have never encountered a competitive situation where one business entity has such a staggering competitive advantage over other entities. I am unaware of any other competitive environment where competitive advantages would be considered so great that competitors would have absolutely no strategic answer except perhaps liquidation of assets. Such an advantage can only occur through government decreeing that business practices currently illegal to all are suddenly legal – but only for one competitor – which is precisely what the Casino Compact did.

Authors notes:

1. All statistics were taken from the SGC's own SEC filings. For other statistics, sources are listed.
2. I have received no compensation monetarily or otherwise in any form for performing these analyses.
3. It must be noted that the SGC is not responsible for creating these competitive conditions. They are merely taking advantage, as any business would, of what strategic options are open to them. For culpability look to the politicians at both the state and local level who supported the project and pushed it forward without performing due diligence on the legality as well as the economic impacts of it.

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