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Gaming Board Rolled the Dice on Pittsburgh's Casino License

The financial situation of PITG Gaming is looking shaky and is casting doubts on the firm's ability to construct a slots parlor on the City's North Shore. While financial concerns dogged PITG in the months leading up to its selection to receive the City's stand alone slots license from the Pennsylvania Gaming Control Board (PGCB), recent revelations may put the project in jeopardy.

In 2006, three applicants for Pittsburgh's slots license under went intense scrutiny from the Gaming Board as well as from the media. It was revealed that Don Barden's Majestic Star Casino LLC, the parent company of PITG Gaming, was experiencing financial difficulty with some of its casinos in Indiana, Mississippi, and Colorado. Shortly after winning the license, it was revealed that Majestic Star lost $9.5 million in the final quarter of 2006. They also lost $4.7 million in profits during the first quarter of 2007 due in large part to an 8.9 percent decrease in revenues.

Despite these losses by Majestic Star, the Control Board had this to say in February 2007: "Because PITG Gaming is a newly-formed entity with no financial history, the PGCB Financial Suitability Task Force analyzed the past financial performance of the Majestic Star Casino, LLC, a wholly owned subsidiary of Barden Development, and did not find anything financially material that would preclude PITG Gaming from obtaining a …slot machine license." Unfortunately, their finding that nothing would preclude PITG from getting the license is a weak endorsement. One would hope the Board would have required strong financial conditions from any applicant chosen to receive a license.

However, Standard and Poor's (S&P) now offers a different perspective. In a report released in late April 2008, S&P assigned a low credit rating to Majestic Star dropping it from a B minus to CCC plus. S&P based the rating on ongoing fiscal woes facing Majestic Star noting $26.1 million in losses during 2007 with debt of $556.7 million.

As for the newly-formed entity PITG Gaming, S&P assigned it a B minus credit rating as well and "suggests that the project is highly vulnerable." This vulnerability, according to S&P analysts, is due to a lack of equity in the project as PITG is relying entirely on borrowed funds. The first borrowing of $200 million, used to begin construction, is due in May 2008. PITG is scrambling to borrow more money to pay that loan off and to secure more funds to pay for the rest of the project, which has seen cost rise from the initial $450 million to a now estimated $770 million when all costs including 40 percent higher construction costs, legal fees, the license fee, and other "soft" costs are added.

Barden recently appeared before the Gaming Board to ask for changes to his casino plan, some of which reflect the company's recent financial difficulties. Originally he had indicated that a Wall Street firm would provide $450 million to finance the project. He is now asking that he be permitted to take three separate loans totaling $800 million. In light of the very low credit rating of both the Majestic Star LLC and PITG Gaming, his interest rate on bank borrowing could be as high as 16 percent.

While most believe Pittsburgh's stand alone casino will generate significant revenue, it may not be enough to satisfy the credit market *and* all of the promises Mr. Barden made to secure the license. Original projections for Barden's casino placed daily per machine revenue at $276. With 3,000 machines initially, that would produce just over $300 million annually in total casino revenue. Of course, out of this $300 million, state and local governments will take approximately 44 percent leaving Mr. Barden with $168 million. From this net figure he has committed $7.5 million per year for the new Penguins arena and $1 million per year for three years to Hill District developments.

Out of the remaining revenue, Mr. Barden will have to pay debt service on the projected borrowing that could easily run between $90 and $100 million annually even assuming the most favorable interest rates. Undoubtedly, considering credit market conditions and the big jump in additional borrowing, the new debt service figure is vastly higher than the number projected when the expected cost was $450 million. Whatever profits he had hoped to get from this project will be greatly diminished, if they do not disappear altogether, with the massive increase in debt service payments.

Realizing this, Mr. Barden had recently asked the Gaming Board to reconsider his proposal to invest $3 million in seed money to redevelop the Hill District—a commitment he has subsequently assured community leaders will still be forthcoming. Will he also beg out of his annual $7.5 million commitment to help build the new arena? The County Executive claims he is not worried about this turn of events—he believes the Gaming Board will handle it.

But given how poorly the Gaming Board has handled things to this point, not only should the Chief Executive be worried, but anyone with a stake in the success of this casino should be worried as well. After all it appears that the Gaming Board granted a license to an applicant who has put absolutely no equity in the project, violating all reasonable guidelines for issuing a valuable state franchise. What's worse, apparently even the $50 million license fee was borrowed. What could the Gaming Board have been thinking? They were supposed to make sure the applicants were not only free of criminal records but financially viable as well. It appears they were derelict and haphazard in their evaluation of PITG's financial conditions. The consequences could turn out to be dreadful for all concerned.

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