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**4 July 2013**

## CROWN SYDNEY HOTEL RESORT UNSOLICITED PROPOSAL UPDATE

**MELBOURNE: Crown Limited (ASX: CWN)** announced earlier today that it has been invited by the New South Wales Government to move to Stage Three of the Unsolicited Proposal process for a six-star hotel resort including VIP gaming facilities at Barangaroo South.

In addition to the materials provided to ASX earlier this afternoon, Crown now attaches the following documents:

1. Unsolicited Proposal, Report From Steering Committee, Assessment of Crown and Echo Proposals, Summary of Findings, July 2013;

2. Unsolicited Proposal, New South Wales Government Assessment Report, Crown Sydney Hotel Resort, Stage 2, July 2013; and

3. Key Attributes of the Crown Sydney proposal.

A copy of the Crown Sydney Hotel Resort Project Submission (Volume 1A – 1D) will also be placed on the Crown Limited website.

As a consequence of the release of the attached information, Crown will now request that the trading halt, which was implemented earlier today be lifted.

**ENDS**

**COPIES OF RELEASES -** Copies of previous media and ASX announcements issued by Crown are available at Crown's website at www.crownlimited.com

Unsolicited Proposals

# REPORT FROM STEERING COMMITTEE

## ASSESSMENT OF CROWN AND ECHO PROPOSALS

SUMMARY OF FINDINGS

JULY 2013

# EXECUTIVE SUMMARY

A Government appointed Assessment Panel and an independently chaired Steering Committee have completed their Stage 2 assessment of the proposals submitted by Crown Ltd (Crown) and Echo Entertainment Group Ltd (Echo), consistent with the requirements of the NSW Unsolicited Proposal Guidelines.

This Report presents the summary of findings and recommendations from the parallel assessment processes.

After considering the Stage 2 proposals received on 21 June 2013, we concur with the Stage 1 conclusion that the two proposals are mutually exclusive. This is because both of Echo's proposed options seek exclusivity in a form that would not permit the Crown proposal to proceed.

Both the Crown and Echo proposals, supported by the analysis conducted by Deloitte Access Economics, confirm that:
Sydney is falling short of its potential share of a rapidly growing international gaming and tourism market
Sydney has underperformed compared with Melbourne, even though the single casino in Melbourne does not have exclusivity
To be competitive requires an investment in integrated resort style facilities taking advantage of special locations, and
The Pyrmont, Darling Harbour and Barangaroo precincts have the potential to become a virtual integrated resort, with a unique location on Sydney Harbour.

The Steering Committee believes that Sydney and NSW would derive greater benefit through a competitive casino market which delivers increased tourism and visitation as well as broader economic benefits. This will need to be managed by appropriate safeguards that minimise problem gambling.

This means, given the nature of the proposals and our assessment findings, that Crown should be offered the opportunity to move to Stage 3 with conditions. Establishing a competitive gaming market in NSW, with the attendant need for competitive neutrality would mean that there are a number of issues for the Government to consider if it accepts this recommendation. Clear negotiating parameters would be required for Stage 3. These are dealt with in this report below.

The Steering Committee believes that the recommendations, if adopted, would not exacerbate problem gambling associated with casino operations in NSW. Central to this is ensuring that the proposed commitments to responsible gaming programs are performed by operators. The Committee also recommends that additional third party exclusion measures to protect families be considered by Government.

David Murray AO

Steering Committee Chairman
July 2013

# 1 ASSESSMENT PROCESS

A Government Assessment Panel and an independently chaired Steering Committee have completed their Stage 2 assessments of Unsolicited Proposals from Crown Ltd and Echo Entertainment Ltd, consistent with the requirements of the NSW Unsolicited Proposals Guidelines.

Given the high level of public interest in casino style gambling and with development at Barangaroo, the Government appointed eminent independents to serve as Chairman of the Steering Committee and as a Probity Adviser after Crown's proposal was approved to progress to Stage 2 on 24 October 2012.

The Chair has been David Murray AO, former Chief Executive Officer of the Commonwealth Bank and Chair of the Australian Future Fund. The Probity Adviser has been the Hon. Ken Handley AO OstJ QC, a recently retired judge of the NSW Court of Appeal. Both agreed to extend their roles when Echo made its submission 3 April 2013 and Government approved progression to Stage 2 on 8 April 2013.

Mr Handley's probity report (attached) confirms that the Stage 2 assessment has been carried out by the Panel and Committee with transparency and fairness to both proponents, and with appropriate thoroughness and rigour in the interests of the State.

The assessment process has included 20 meetings with each proponent, and 2 meetings with the Chairs of the Steering Committee and Assessment Panel to review preliminary final proposals and identify key assessment issues.

A critical assessment of the business models from both proposals has been undertaken by the Panel, with the assistance of Deloitte Access Economics (Deloitte), to ensure that they are robust and that their forecasts for growth in markets, revenue and tax are credible.

It is important to understand that the assessment process is not the same as a tender evaluation. The Unsolicited Proposals Guidelines set out seven evaluation criteria, listed below. In this case, the two proposals are for different projects, with different requests of Government, and there is an established one–casino market to take into account.

Under the Unsolicited Proposals Guidelines, each proposal is assessed on its individual merits, in order to determine whether it would merit progression to Stage 3. The Steering Committee has overseen the parallel assessment of both proposals.

As the Stage 1 assessment of Echo's proposal (which was received after Crown's proposal) found that the two proposals were mutually exclusive, the Committee has also prepared advice for the Government on the options available to it under the Unsolicited Proposals framework. This Report contains the advice.

The Assessment Panel's Reports on each proposal, including economic assessment from Deloitte, have been prepared for public release alongside both proposals.

The Unsolicited Proposals process does not substitute or pre–empt any required legislative, regulatory or planning approvals, or the public consultation involved in each. These stages would follow any government agreement for a proposal to move to Stage 3.

# 2 CROWN PROPOSAL ASSESSMENT SUMMARY

Crown proposes to invest approximately $1.3billion to construct an iconic 6 star hotel and apartment building at Barangaroo South, including a VIP gaming facility. Crown seeks a VIP gaming licence to enable the project to proceed. The table below summarises the assessment of Crown's proposal against the criteria for assessments of Unsolicited Proposals.

| UNSOLICITED PROPOSAL ASSESSMENT CRITERIA | ASSESSMENT OF CROWN'S PROPOSAL |
|---|---|
| **Uniqueness** | • Unique because Crown has secured an exclusive right to develop an iconic hotel in Barangaroo South. |
| **Value to Government** | • Crown offers an upfront licence fee of $250million or $100million, with tax rates of 9% or 10% for rebate play and 23% or 27.5% for non–rebate play.<br>• Assessed increase in Gross State Product (GSP) of $442million per annum in 2025.<br>• Assessed net present value (NPV) of extra tax and licence fee revenue of $441million to FY2035.<br>• Investment of $1.3billion in construction and development<br>• 1,250 additional direct jobs after construction.<br>• Introduction of competition increases growth prospects for the gaming and tourism industries. |
| **Whole of Government Impact** | • Substantial contribution to international tourism growth, with a focus on high net worth Asian gaming market and local VIPs<br>• Potential additional social harm from problem gaming is mitigated by exclusion of poker machines, minimum bet limits and membership entry requirements. Membership criteria need development.<br>• Proposed tax rates that are inconsistent with competitive neutrality at current rates.<br>• Requires change to legislation and development approval.<br>• Principal opportunity cost is forgoing Echo's proposed $250million payment over 21 years to renew exclusivity. |
| **Appropriateness of Return, considering risks** | • Indicative project returns for the company are not excessive. |

Crown's submission estimates an addition of $638million per annum to GSP in the first full year of operations (FY22). This has been scaled back to $388million in FY22 ($442million in FY25) following assessment because its forecast for growth rates for The Star under 'business as usual' is considered to be low. These adjustments also produce a proportional reduction in tax forecasts, producing an NPV of licence fee and tax of $441million to FY2035.

The estimate of Crown's contribution to GSP includes no provision for spending by its customers outside its premises, or for the benefits of investment that Echo might reasonably make in response to the introduction of a competitor.

Sydney has underperformed compared with Melbourne, where Crown operates a single casino that does not have exclusivity. Crown has continuously re–invested in its facilities and has achieved total revenue over 60% greater than The Star. This indicates a track record of successful and consistent operations by Crown, which adds confidence that its proposed investment should benefit NSW.

Crown has proposed two licence fee and taxation options. One offers a higher up–front licensing fee of $250million, while the other offers higher ongoing tax rates of 10% for rebate play and 27.5% for non–rebate play with a licence fee of $100million. Recommendations regarding tax options are included below.

| UNSOLICITED PROPOSAL ASSESSMENT CRITERIA | ASSESSMENT OF CROWN'S PROPOSAL |
|---|---|
| **Capability** | • Delivery of the proposal is clearly within the assessed capabilities of Crown. |
| **Affordability** | • Neither Government nor taxpayers are making any contribution to the project cost.<br>• The Government has incurred the cost of the assessment process. |
| **Risk allocation** | • Investment and project risk is appropriately retained by Crown.<br>• Risk of revenue falling below forecast levels is considered to be low based on anticipated growth in the international gaming market.<br>• Introduction of competition reduces the risk that Sydney will continue to underperform in this industry compared to competing cities. |
| **Recommendation** | • Merits progression to Stage 3 if the conditions as recommended in Section 6 are agreed by Crown. |

# 3 ECHO PROPOSAL ASSESSMENT SUMMAR

Echo proposes to invest $1.1 billion to create an integrated resort on its existing site at Pyrmont, including public domain investment for a pedestrian bridge to Barangaroo, embellishment of waterfront parks and walkways, and an upgrade of the light rail station. Echo seeks a 15 year extension of The Star's exclusivity arrangement to provide certainty for its investment.

The table below summarises the assessment of Echo's proposal against the criteria for assessments of unsolicited proposals.

| UNSOLICITED PROPOSAL ASSESSMENT CRITERIA | ASSESSMENT OF ECHO'S PROPOSAL |
|---|---|
| **Uniqueness** | • Unique because Echo already holds the State's only casino licence and no other party could apply for an exclusivity agreement. |
| **Value to Government** | • Echo proposes $250million for renewed full exclusivity or $0 for renewed partial exclusivity. Both options also seek a $250million per annum increase in the threshold at which rate escalation begins (for non–rebate, ie local play).<br>• Assessed increase in GSP of $350million per annum in 2025.<br>• Estimated net present value of extra tax and licence fee revenue of $337million to FY2035.<br>• Investment of $1.1billion in construction and development, including $130million for public domain<br>• 1,460 additional direct jobs after construction. |
| **Whole of Government Impact** | • Substantial contribution to international tourism growth, with a focus on middle class Asian tourists, high net worth Asian international VIPs, and interstate tourists.<br>• Potential to increase problem gambling as Echo proposes to raise [redacted] million pa extra from poker machines by removal of $10 maximum bet limits on 1,250 machines.<br>• Requires development approval.<br>• Principal opportunity cost is forgoing benefits of Crown's proposed investment, potentially partly substituted by construction of a lesser hotel at Barangaroo. |

| UNSOLICITED PROPOSAL ASSESSMENT CRITERIA | ASSESSMENT OF ECHO'S PROPOSAL |
|---|---|
| **Appropriateness of Return, considering risks** | • Indicative project returns for the company are not excessive. |
| **Capability** | • Delivery of proposal is within the assessed capabilities of Echo. |
| **Affordability** | • Neither Government nor taxpayers are making any contribution to the project cost.<br>• The Government has incurred the cost of the assessment process. |
| **Risk allocation** | • Investment and project risk is appropriately retained by Echo.<br>• Risk of loss of existing forecast potential tax revenues is considered to be low.<br>• Proposed investment by the proponent reduces the risk that Sydney will continue to underperform in this industry compared to competing cities.<br>• Government bears reputational risk if public domain investments are not executed. |
| **Recommendation** | • If Government decides to retain a one–casino model, proposal merits progression to Stage 3 if the removal of bet limits on poker machines is limited to VIP or other approved private areas. |

Echo has proposed that its project would add $350million per annum to NSW GSP in 2025. Our analysis supports this. Its NPV of extra tax and licence fee revenue is assessed at $337million to FY2035.

The Committee believes that Echo's proposal represents a more sophisticated integrated resort model than its more recent investment to upgrade The Star, and materially expands its existing hotel room numbers. The Committee think it is likely that Echo would be motivated to undertake at least some of its published strategic investment plans in response to the introduction of competition, whether its proposal was successful or not.

# 4 COMPARATIVE EVALUATION

Both proposals meet the three qualification criteria and perform satisfactorily against the four performance criteria as required under the NSW Government Unsolicited Proposal Guidelines. However, as both of Echo's options require exclusivity in a form that is incompatible with Crown's proposal to include domestic VIP gaming, the proposals are mutually exclusive and therefore only one can proceed.

The economic assessment observes that Crown's contribution to GSP is 26% larger than Echo's in FY2025 and that Crown's NPV of extra tax and licence fee revenue are 31% larger than Echo's, respectively. The Committee is satisfied that the modelling and analysis have been conducted in a robust and consistent way to enable reliable comparison of economic and taxation outcomes from proposed investments.

However, the Committee is cognisant that the indicated results ultimately depend on whether the proponents are successful in achieving projected growth. This will be determined by the quality of their strategies, execution, resilience and wider market conditions. For this reason, assessed impacts on GSP and taxation revenue are not considered a sufficient basis alone for selection between the two proposals.

Comparison of the proposals has focused on achieving the best outcome for NSW. Both proposals and the assessment, supported by the analysis conducted by Deloitte, confirm that:

- Sydney is falling short of its potential share of a rapidly growing gaming and tourism market
- Sydney has underperformed compared with Melbourne, even though the single casino in Melbourne does not have exclusivity
- To be competitive requires an investment in integrated resort style facilities taking advantage of special locations, and
- The Pyrmont, Darling Harbour and Barangaroo precincts have the potential to become a virtual integrated resort, with a unique location on Sydney Harbour.

The Committee therefore believes that the decisive factor in the choice between Crown's and Echo's proposal is the opportunity to introduce competition.

# 5 ISSUES FOR THE STATE

## COMPETITION

The presence of a second casino will create sustained incentives for improvements in performance, making Sydney more attractive to tourists overall. The cities that are most notably successful in the global gaming markets (Macau, Singapore, and Las Vegas) all have more than one casino, with differentiated offerings targeting different market sectors.

NSW currently operates a one casino model. Accordingly the transition to competition requires adjustments to taxation and regulatory settings to establish a level playing field which is also conducive to investment and growth.

## TAXATION

Crown has proposed two taxation options, and neither is wholly consistent with existing rates.

In the category of international and interstate rebate based play. Crown's 10% flat tax option is the same as at The Star, and would thus deliver competitive neutrality.

In the category of non–rebate based play, Crown's 27.5% option is equal to the base tax rate paid at The Star. However, The Star is subject to marginal rates that will rise to 50%. The Committee recommends that non–rebate based play should be taxed at a flat rate to maintain competitive neutrality. The majority of the Committee, including the Chair, support a flat rate of 29% which will provide an environment conducive to investment and growth, without material risk to taxation revenue. The alternative view was the flat tax rate should be 31% which would provide the State with a better share of any potential upside in the casino gambling market. These tax rates are inclusive of GST of 9.09% and the Responsible Gambling Levy of 2%. The Star will be transitioned to the same flat rate when its exclusivity period ends.

## GAMING REGULATION AND PROBLEM GAMBLING

The Committee has sighted evidence from the Productivity Commission that the social impacts of casino gaming can be managed through responsible gaming measures and minimising reliance on mass market poker machines.The Committee has noted that both proposals include a commitment to deliver substantial responsible gaming programs. It recommends that the Government also consider establishing a third party exclusion program to protect families at casinos in NSW, as has been adopted in ACT, South Australia and New Zealand.

The issue of VIP definitions has been contested in the proposals. It is a relevant matter for determination of taxes and licence fees, and to prevent a gradual expansion of gaming beyond the VIP market sector that Crown has proposed to serve. The Committee has included recommendations to better define VIP Gaming.

## GOVERNMENT LEGAL, FINANCIAL AND REPUTATIONAL RISK

There are important risks for the Government to consider. Issues connected with competition, social harm, and taxation are considered above. Other risks are:

*Planning approvals*. While not a matter for the Committee to determine, obtaining planning approval is a risk that must be retained in full by Crown. Crown's current proposed building is materially taller than the site's existing approved envelope. It would be up to Crown to ensure that any reduction required by the planning decision–maker in the numbers of floors, hotel rooms or apartments could be accommodated.

*Completion risk* (contractual and project). Approval and execution of the proposal is complex. Most of the risks will be borne by Crown. Stage 3 documentation should be structured with particular care to ensure that the State's interests are protected. This would include early payment for a gaming licence, once granted, as proposed by Crown.

*Legislative risk*. The Casino Control Act 1992 will need to be amended to remove the one casino policy.

In a competitive setting, there will be a higher likelihood of project commitment and delivery. The business model adopted elsewhere by Crown, and its success in Melbourne, gives confidence that its project will be completed.

# 6 STEERING COMMITTEE RECOMMENDATIONS TO GOVERNMENT

## 1. ESTABLISH COMPETITION AND DO NOT EXTEND EXCLUSIVITY

Echo's proposal to extend exclusivity until 2034 is not consistent with establishing competition, and should therefore not be progressed. Nevertheless, in pursuing regulatory reforms to establish competitive neutrality, the Government should consider ways in which Echo would be incentivised to invest in The Star without compromising the State's position on tax revenue and problem gambling.

## 2. OFFER CROWN THE OPPORTUNITY TO MOVE TO STAGE 3 WITH CONDITIONS

Crown's proposal for VIP gaming, with an upfront licence fee of $100million (paid within 20 business days of issuing the licence) and a tax rate for rebate based play of 10% (including GST), should be progressed to Stage 3 with four additional conditions. The conditions for moving to Stage 3 are:

- Adopting the majority position of the Steering Committee that non–rebate play would be taxed at 29% (including GST and the responsible gaming levy) not 27.5% as proposed by Crown, and
- The total of licence fee and gaming tax payments to NSW over the first 15 years of full operation must exceed $1billion (nominal), a guarantee Crown proposed for its alternate option, and
- Licence fee and tax would be reviewed after 20 years of operation, having regard to market conditions, financial viability and competitiveness, and the licensee earning a fair return on capital. Timing for the review of both casinos will be aligned, and
- Local VIP membership criteria must include a 24 hour cooling off period for applicants who cannot demonstrate a track record of VIP gaming at other casinos, rules to ensure that guests are bona fide, and regular reviews of members gaming to ensure that they should remain as members.

For clarity, Crown should also be asked to confirm the Committee's understanding of the Crown proposal in relation to the following matters:

- The costs of regulation of Crown Sydney will be met by Crown. The Independent Liquor & Gaming Authority (ILGA) will determine day to day regulatory requirements and investigate a system of third party exclusion procedures, to protect families, which will apply to all casinos in NSW.
- The approach to regulation of the two casinos in NSW will be consistent (including front money for rebate play) and that the Government will initiate a review of regulatory efficiency to ensure that contemporary, effective and productive procedures are employed and continually refined.

As advised, Crown is requested to pay the Government a non–refundable $5 million deposit to enter into Stage 3, which would be credited against its licence fee payment if a licence is granted.

## 3. IF CROWN DOES NOT ACCEPT THE OFFER, GO TO TENDER

If the above conditions are not accepted by Crown, then the Government should consider conducting a tender process for a licence to establish a second gaming and tourism resort in Sydney.

The Hon Ken Handley AO, OstJ, QC

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Joint Steering Committee for the
Crown Sydney Resort Project & Echo Entertainment Group Ltd
Department of Premier & Cabinet
1 Farrer Place
Sydney NSW 2000

Dear Committee members

**Probity Report on the Assessment of Stage 2 Unsolicited Proposals from Crown Limited and Echo Entertainment Group Limited**

On the 24 of October 2012 Cabinet decided that the unsolicited proposal received from Crown Ltd on 6 September should proceed to Stage 2 assessment under the Government's Guidelines for such proposals. On 5 February 2013 I was appointed as the Probity Adviser to the Steering Committee chaired by Mr David Murray AO, and the Assessment Panel chaired by Mr Simon Smith of the Department of Premier and Cabinet replacing the previous Probity Adviser.

Since my appointment I have attended all meetings of both bodies except those between 16 May and 18 June when I was traveling under arrangements made before my appointment which were disclosed to Mr Simon Smith at the time. While I was away I remained in email contact with members of the Panel and Committee, receiving 36 emails and sending 19.

I initially focused on 2 issues. Did Crown have the legal rights it claimed over the Barangaroo site which "uniquely" entitled it to make its unsolicited proposal under the Guidelines? Secondly did Deloitte Touche Tomatsu Australia(Deloittes), the adviser to the Committee and Panel on accountancy and taxation aspects of Crown's proposal , possibly have a conflict of interest ? Such a possibility may have arisen because a subsidiary of Crown owns 33.3% of the issued shares in Melco Crown Entertainment Ltd of Macao (Melco) and Deloittes China are the external auditors of Melco.

I was aware of comments in the Press prior to my appointment suggesting that the relationship between the Deloitte firms created a conflict of interest. I also considered that the contractual restraint on Deloittes against accepting professional engagements from Crown and related companies was too short.

I asked representatives of Crown at meetings of the Panel for a copy of the agreement between Lend Lease and Crown which was said to give Crown the exclusive right to develop the Barangaroo site, but for some time could only obtain a redacted copy which was useless for my purpose. Crown was in a difficult position because it was contractually bound to treat the agreement as confidential, and Lend Lease would not allow disclosure of the whole document. Mr Murray and I insisted on disclosure and Lend Lease eventually agreed to our inspecting it at their office in the presence of their in-house counsel, under obligations of confidentiality. I was therefore able to satisfy myself that Crown had the exclusive development right it claimed.

The agreement between the Government and Deloittes prevented the firm accepting engagements from the Crown group as long as they were working for the Government on this

project. I considered that this gave the Government inadequate protection from the appearance of conflict that would arise from an engagement of the firm by Crown shortly after it completed work on this project. I hasten to add that I had no reason to suspect that Crown would offer such an engagement or that Deloittes would accept it. Moreover to my observation their partners and staff working on this project acted throughout with professional skill and integrity in the interests of the State. Nevertheless I was concerned that such an engagement, however unlikely, would raise doubts in the mind of the public about the independence and rigour of their work and create the appearance of a conflict of interest.

Accordingly I advised the Steering Committee that Deloittes should be asked to accept a restraint against such engagements for a further 2 years. When Mr Murray intervened they accepted a restraint for two.

My other concern related to the position of Deloittes China as auditor of Melco. I was informed that the Australian firm had no interest in that firm or in that audit, and the firms were completely independent. I sought documentary verification and eventually was given a copy of the Articles of Association of Deloitte Touche Tomatsu Ltd, a company limited by guarantee incorporated in the United Kingdom. The various Deloittes firms worldwide are members of this company and its articles of association govern the relationship between them. I checked the articles and read documents generated by the firm's conflict management department in 2012 in which they concluded that the position of the China firm did not create any conflict which could prevent the Australian firm examining Crown's then relationship with Echo through its 10% shareholding, or Crown's unsolicited proposal. I was satisfied that Deloittes had no right to share in the profits of the China firm and no responsibility for its liabilities and it had no conflict of interest in carrying out its retainer for the review of the Crown and Echo proposals.

The agenda papers for all meetings of the Panel and Committee without representatives of Crown or Echo being present included provision for disclosures of any conflicting interest. Some disclosures were made out of superabundance of caution, such as living in Pyrmont, but these did not reveal any reason for doubting the integrity and impartiality of those concerned. Nothing came to my attention at any stage which suggested that any of the persons on the Government side had an actual or possible conflict of interest.

Having attended all meetings of both committees since my appointment, apart from those while I was out of Sydney, and been kept informed of relevant developments during my absence, I am satisfied that the assessment process for both proposals has been conducted on the Government side thoroughly and with rigour with a view to securing the best possible financial result for the State. The rigour of the process was enhanced when Cabinet decided that Echo's unsolicited proposal of 3 April.

2013 should be taken through the Stage 2 process by the same Steering Committee and Assessment Panel. Echo's only proposal at that time was inconsistent with Crown's and introduced an element of competition which could not be present when a single unsolicited proposal was being considered.

Some of aspects of the final proposals are a substantial improvement on those originally foreshadowed by the proponents, and have been included despite earlier resistance to suggestions from the Panel or the Committee that they were appropriate. I am satisfied that the assessment for Stage 2 has been carried out by the Panel and Committee with transparency and fairness to both proponents, and with appropriate thoroughness and rigour in the interests of the State.

Yours sincerely

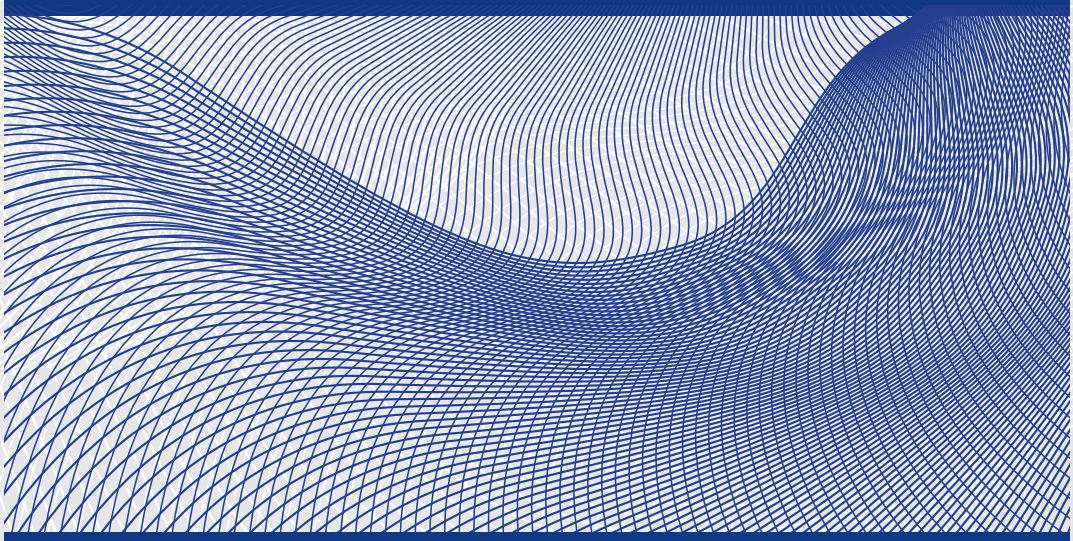
The Honourable K R Handley AO OStJ QC.

UNSOLICITED PROPOSAL

# ASSESSMENT REPORT

# CROWN SYDNEY HOTEL RESORT

STAGE 2



JULY 2013

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# 1 INTRODUCTION

This Assessment Report considers the Unsolicited Proposal received from Crown Ltd (Crown) that proposes construction of a 6 star hotel resort, including VIP gaming, at Barangaroo South.

This Assessment has been conducted by the NSW Government and overseen by an independently chaired Steering Committee in accordance with the NSW Government Unsolicited Proposals Guidelines, 2012.

This Chapter explains the Unsolicited Proposal process, the decision makers and the opportunities for the community and stakeholders to have their say in the next steps.

## Encouraging innovative ideas from the private sector

The NSW Government established an Unsolicited Proposal process in 2012 to encourage ideas from the private sector that could provide benefits to the people of NSW.

The Guidelines for the submission and assessment of Unsolicited Proposals sets out a structured and streamlined approach for the NSW Government and the private sector to work together to consider innovative ideas. The Unsolicited Proposal process involves three stages.

**Stage 1** — Initial Submission and Strategic Assessment, includes a comprehensive initial assessment of the proposal to identify the potential benefit to Government of further consideration and development with the Proponent. The Crown Unsolicited Proposal progressed successfully through this stage in October 2012.

**Stage 2** — Detailed Proposal, requires the Proponent and Government to work co-operatively in the development and assessment of a Detailed Proposal. This document is the Assessment Report for Stage 2 of the Unsolicited Proposal process. The outcome of Stage 2 is a decision to progress to Stage 3, or that the Government does not wish to proceed.

**Stage 3** — Negotiation of a Final Binding Offer, involves the finalisation of all outstanding issues with a view to entering into a binding agreement, should the Government accept the final offer. None of the above replaces the normal processes of legislation, development assessment or regulation. If a proposal completes Stage 3, these processes if required (including public consultation) will then commence.

## Unsolicited Proposals must provide unique benefits to NSW

Unsolicited Proposals need to provide unique benefits to justify direct negotiations between Government and the private sector. The Government's preferred position as stated in the Guidelines is to test the market to maximise value–for–money outcomes and to provide fair and equal opportunities. Therefore Unsolicited Proposals are rigorously assessed against the following criteria:

- Unique benefits of the proposal — such as property ownership or intellectual property
- Value to Government — including economic benefit, improved service delivery, whole–of–life costs, risk transfer, timely achievement of objectives and qualitative outcomes
- Whole–of–Government impact, including opportunity cost
- Appropriateness of return on investment obtained by the Proponent given project risks
- Capability and capacity of Proponent to deliver the proposal
- Affordability, and
- Appropriate risk allocation.

The subsequent chapters of this Report assess the Crown proposal against each of these criteria.

## A robust assessment process has been implemented

A Steering Committee was established for consideration of the Unsolicited Proposals. The Committee members are Mr David Murray AO, the independent Chair, the Director General Department of Premier & Cabinet (DPC), Secretary NSW Treasury, and the Director General Department of Trade and Investment, Regional Infrastructure and Services (DTIRIS).

The Steering Committee is supported by an Assessment Panel with the following membership:

- Deputy Director General, DPC (Chair)
- Deputy Secretary, NSW Treasury
- Acting Deputy Director General, DTIRIS.

The Hon. Ken Handley AO OstJ QC provided probity supervision and advice during the Stage 2 process.

During the Stage 2 assessment, the Assessment Panel held 20 meetings with representatives of Crown to work co-operatively on the development of the Detailed Proposal. The Chair of the Steering Committee also met with Crown representatives twice to receive a briefing on the preliminary final proposal and identify key issues for the assessment.

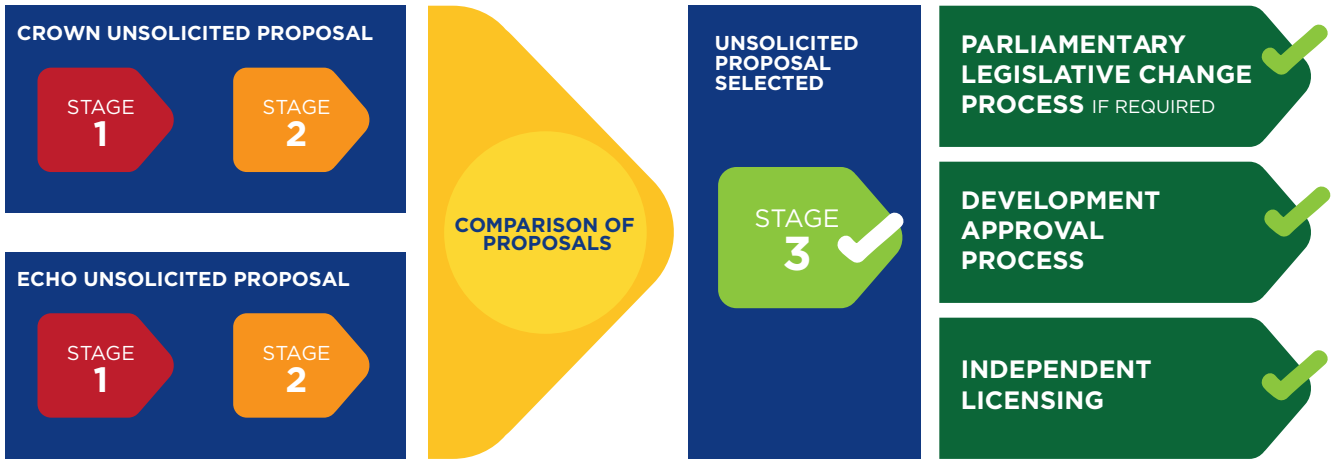
## The assessment precedes normal approvals and consultation

A proposal that successfully makes it through the Unsolicited Proposal process is still required to go through all relevant approval processes including:

- Parliamentary processes for the change of legislation, if required
- Planning development assessment approval process including community consultation, and
- Independent licensing process, if required.

These processes include consultation with stakeholders and the community.

The process for the assessment of the Crown proposal is illustrated as follows:




**STAGE 1**
Steering Committee agree proposal meets criteria for assessment as an Unsolicited Proposal

**STAGE 2**
Steering Committee considers detailed proposals and suitability for progression to Stage 3

Steering Committee compared mutually exclusive proposals. Only the proposal which best meets the criteria progresses to Stage 3.

**STAGE 3**
Government decides whether to accept a final binding offer.

The proposal is then subject to all relevant approval processes, including consultation with stakeholders and the community.

# 2 GAMBLING AND GAMING IN NSW

This Chapter explains the current policy settings and legislation for gambling and gaming in NSW. A comparison is made between NSW and other jurisdictions in Australia and overseas.

## The Star City casino has exclusivity until 2019

In December 1994, the NSW Government issued a 99-year casino licence and The Star City Casino subsequently opened in Pyrmont with exclusivity until 2006. A payment for $376million was made to the NSW Government, comprising $256million for the casino licence and $120million as pre-paid rent for the first 10 years usage of the casino site leased from the State.

In 2008 the Government extended the exclusivity agreement with Echo, the operator of The Star Casino at Pyrmont, until November 2019, and received an additional licence fee of $100 million. The exclusivity agreement imposes penalties on the NSW Government should it permit casino type gaming to be undertaken at another site before 14 November 2019.

## Gambling is a large industry in Australia

Gambling is a common recreational pursuit in which around 70% of Australians participate. Australia wide, gambling expenditure is $18.2 billion per annum and in NSW gambling expenditure is $7.4 billion per annum (2011–12).

More than half this revenue comes from electronic gaming machines (mainly poker machines and some from electronic versions of casino table games). Casino gaming makes up 18% of the gambling expenditure across Australia, but only 10% in NSW.

There are now 13 casinos in Australia. The largest casino is Crown Entertainment Complex in Melbourne. Queensland has four casinos, Northern Territory and Tasmania each have two casinos and the remaining States and the ACT all have one casino.

The casinos in Australia are not only competing with each other to attract interstate and international players, but also with significant existing and new casino and resort facilities in Singapore, Malaysia, Manila, Macau and Las Vegas.

## Potential exists for substantial market growth

The international VIP gaming market is experiencing high growth originating in Asia. Accepted estimates are from $8billion in 2006-7 to $34billion in 2011-12. Australia currently has 3% ($1billion) of this market share, third behind Macau (82%) and Singapore (10%).

Casino gaming is also an attractor for China's growing middle class, who value access to gambling opportunities within an integrated resort that offers a range of leisure and cultural facilities.

## The definition of a VIP player differs

In Australia, play is divided for tax purposes into rebate (low tax) and non–rebate (higher taxed) categories. Lower rates are offered to help Australian casinos compete for highly mobile wealthy customers located in distant markets. Some market participants define these people as 'VIPs'.

Rebate based players are required to deposit money up front to access VIP gaming facilities and benefits. The amount of up–front money in NSW is $75,000 for international VIP players and $25,000 for interstate VIPs. NSW residents cannot participate in rebate based play in NSW.

Other market participants define 'VIPs' to include all individuals who gamble large amounts of money, irrespective of the applicable tax category. From an operational perspective, casinos 'rate' their frequent players based on their expenditure, and 'promote' those who gamble more to 'VIP' gaming areas, where additional incentives and superior facilities are offered.

## There is also great variation in tax rates

Tax is applied to 'gaming revenue', which is the difference between bets placed and winnings paid. Tax rates are normally quoted inclusive of GST.

In NSW, rebate based play is taxed at a rate of 10% (includes GST) and non-rebate based play is taxed on a sliding scale that

commences at 27.5%, rising to a top rate of 50% (includes GST and Responsible Gaming Levy (RGL)). Victoria has higher tax rates on rebate based play, and lower rates on non-rebate based play.

Internationally, the extremes are Macau with a tax rate of 35% and Singapore with a tax rate of 5% of gaming revenue. To compare tax rates fairly, upfront or ongoing licence fees must also be considered.

## Less than 1% of Australians are problem gamblers

Problem gamblers are players that spend more than they can afford without the usual capacity of self–control to correct the behaviour.

The Productivity Commission (2010) has recently reviewed the social and economic impacts of gambling in Australia and concluded that less than 1% of Australians (between 80,000 and 160,000 adults) suffer significant problems from gambling. In NSW the prevalence rate is 0.8%. 230,000 to 350,000 Australians were identified as experiencing moderate risks that may make them vulnerable to problem gambling.

## Electronic gaming machines are the prime source of problem gambling

Electronic gaming machines (mainly poker machines) are the prime source of problem gambling in Australia. Around 4% of Australian adults play poker machines weekly, and 15% of these players are problem gamblers.

The average annual expenditure for problem gamblers is $21,000, 41% of their annual income on average. The social cost of problem gambling is estimated to be at least $4.7 billion per annum in Australia.

## Problem gambling is becoming less prevalent

Over the last decade Governments have put in place an array of regulations and measures to reduce harm to gamblers, with varying degrees of success. There are conflicting views from industry and other organisations around whether the problem gambling prevalence rates have declined but on balance, the evidence suggests that they have fallen.

Pilot government programs (ACT and South Australia) and voluntary programs (run by BetSafe Pty Ltd) have reported some measure of success and a growing acceptance of the value of the third party exclusion programs. Third party exclusions allow family members and/or friends (the third party) of problem gamblers the right to apply for their loved one's exclusion from gambling venues in order to prevent an escalation of their gambling.

# 3 SUMMARY OF CROWN'S PROPOSAL

Crown proposes to develop a 6 star, iconic, luxury hotel resort that includes restaurants, bars, pool and spa facilities, conference rooms, retail outlets and VIP members-only gaming facilities.

This section summarises the two options provided by Crown in its Detailed Proposal and includes:

- The commitments Crown is seeking from the NSW Government
- The commitments Crown proposes to make, and
- The estimated economic and financial benefits, as provided by Crown in their proposal.

Crown's proposal is available at *www.nsw.gov.au/unsolicitedproposals*

## CROWN'S PROPOSAL — OPTION A

Crown proposes to develop a 6 star hotel resort with VIP gaming facilities in an iconic building at Barangaroo South. The building will incorporate 350 hotel rooms and suites and 80 luxury residential apartments, subject to approval.

The proposed location for the development is a waterfront site on the northwest corner of Barangaroo South. The Barangaroo Delivery Authority (BDA) has assigned Lend Lease the right to develop all of the land in this precinct, following a public tender. Lend Lease is also responsible for facilitating 99 year leases between the BDA and future building owners. Crown has signed an Exclusive Dealing Agreement (EDA) with Lend Lease, which entitles it to work with Lend Lease to design and construct the hotel resort. Should the proposal receive approval, Crown anticipates leasing the site from the BDA for 99 years.

The building will be approximately 250 metres high with 70 floors. The proposed site has an area of 6,000 square metres, and will not extend over water. The final dimensions of the building will be agreed in the final design stages. The building is to incorporate the latest energy efficient building practices within the hospitality industry.

The design of the building is looking to achieve the status of a contemporary and iconic landmark. To this end, Crown held an international design competition, obtaining entries from three leading architecture firms in Europe and the US.

The winning design, by Wilkinson Eyre, was announced on 16 May 2013. The jury that made this decision comprised two executives each from Crown, Lend Lease and the Barangaroo Development Authority, as well an independent architect, Roger Poole. Wilkinson Eyre has since been engaged by Crown as the principal architect for the development.

Under Option A, Crown proposes an upfront licence fee of $100million with tax rates of 10% on rebate-based play (which is the same as applies currently at The Star) and 27.5% on non-rebate play (which is the same as the base rate payable at The Star on its first $674million of non-rebate gaming revenue). The 27.5% comprises (16.4% marginal tax rate, plus 2% Responsible Gaming Levy (RLG), plus 9.1% GST). Of this, the GST of 9.09% is payable to the Commonwealth Government.

The NSW Government pays a rebate to The Star on the amount of GST paid to the Commonwealth for rebate gaming revenue.

The Star pays higher rates of tax on its non-rebate gaming revenue above $674million, rising in $5million bands to reach 50% for non-rebate gaming revenue above $792million. The Star has advised that its current average rate of tax (excluding VIP and Domestic Rebate) is now around 28% (includes RGL and GST). The Revenue Thresholds are annually indexed to CPI (as set out in Table 3.1).

## CROWN'S PROPOSAL — OPTION B

Under Option B, Crown's proposal is essentially the same as Option A with an increased upfront licence fee of $250million and a reduced tax rate 9% (including GST) on rebate play and 23% (including GST) on non-rebate play.

### The timeframe for construction is 5+ years

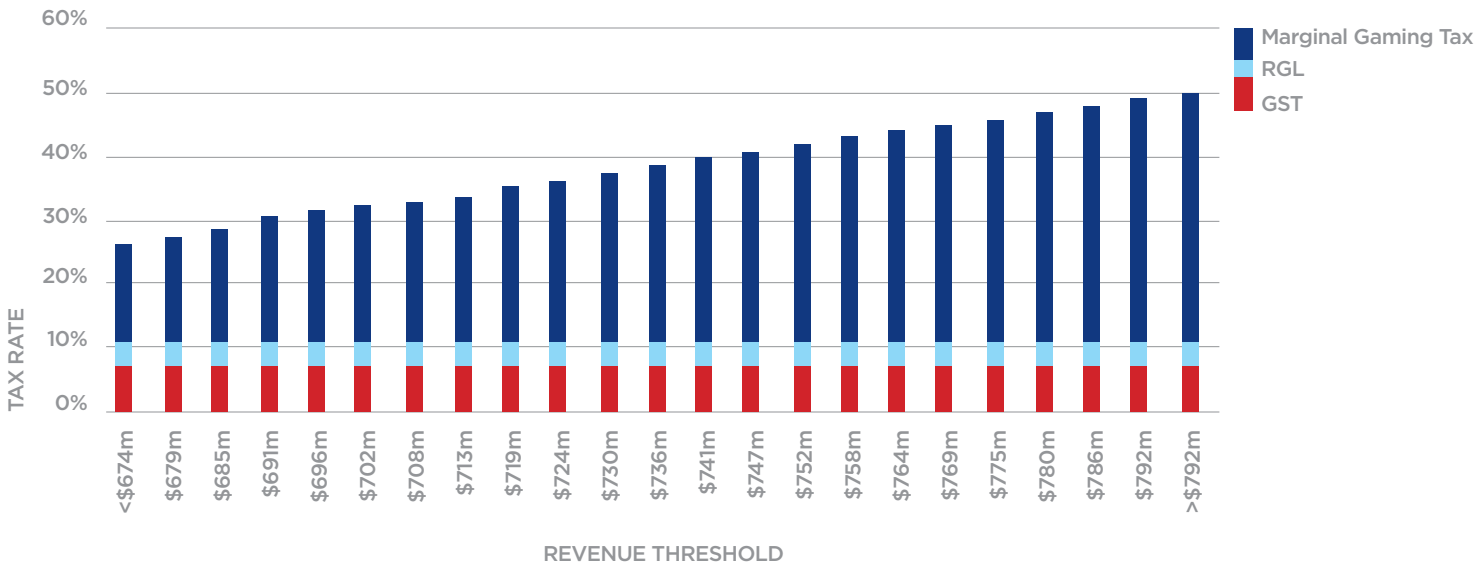
Crown anticipates that it will take between 60-70 months to construct the hotel resort. The hotel resort is expected to open in 2018, with the launch of the VIP gaming facilities following in mid-November 2019 when Star's exclusivity expires (as set out in Table 3.2).

### Links to other resorts and a new training college

Crown proposes to offer high net worth visitors to the hotel resort access to the Ellerston Day Retreat in the Upper Hunter region of NSW, and the Perisher Ski Resort.

It is proposed that guests will be flown to Scone Airport from the Rose Bay terminal in Sydney, and then either driven or flown by helicopter to the Ellerston Day Retreat. The retreat will offer a number of activities including golf at a course designed by Greg Norman and horse riding, along with pool and day spa facilities. Crown Sydney guests that choose to visit Perisher will travel by helicopter from Sydney Airport to an existing helipad nearby the resort. Guests will be offered private guided ski trips and instructor lessons, and will be accommodated at the Perisher Valley Hotel. Crown does not seek approvals for helicopters to access Barangaroo.

TABLE 3.1: 2013 TAX RATES NON-REBATE



Crown proposes to establish training colleges in Penrith and Redfern, in partnership with the Penrith Panthers Group (PPG) and the National Centre of Indigenous Excellence (NCIE). Together, these organisations will establish further partnerships with schools and TAFEs to implement training programs, and establish programs for staff development. While pre–employment training programs will begin closer to the operation phase of the development, there is a possibility that schools–based programs could begin from 2016.

The proposed training college in Penrith will offer apprenticeship, work experience and schools–based traineeship opportunities for local students in year 10 and above. It will also provide cultural programs for Indigenous students and job seekers, and allow staff and students access to the PPG's recreational facilities.

At the NCIE in Redfern, a second training college will focus on pre–employment training, targeting literacy, numeracy and basic employment skills, primarily for Indigenous job seekers, across NSW. It will offer vocational qualifications for students in year 10, 11 and 12, and provide school–based traineeships to Indigenous school students in Redfern, the inner city and Penrith, utilising the NCIE facilities.

Crown is also in the process of developing concepts for other complementary tourist attractions that will contribute to the tourism appeal of Barangaroo.

## 3.1 COMMITMENTS SOUGHT BY CROWN

Crown seeks certainty from the NSW Government in relation to:

- provision and cost of a VIP gaming licence
- resolution of land access issues, and
- taxation and other associated legislation.

### Crown seeks a VIP gaming licence

Crown claims that the proposed 6 star hotel and resort development is not commercially feasible without a gaming component. It is on this basis that the proposal seeks the provision of a VIP only gaming licence from the NSW Government. While no exclusivity agreement is sought for the licence, Crown has proposed a number of licence conditions. These are listed below.

- Access to the facilities will be restricted through a membership system which aims to attract high–spend patrons, similar to that operating in the VIP Gaming areas at Crown Melbourne — entry will not be permitted to the NSW general public unless via the membership system;
- Gaming site will be expressed in terms of total floor space occupied by gaming tables, being the lesser of:
  - 20,000 square metres, or
  - 20% of the final approved total gross floor area of the building;
- An unlimited number of gaming tables will be permitted, and Crown will be permitted to relocate the table games within the building from time to time;
- Low limit table games will not be permitted – defined as a gaming table with a minimum bet limit that is less than the lower of:

TABLE 3.2: PROPOSED TIMING OF THE DEVELOPMENT
SOURCE: CROWN VOLUME 1A – PROJECT SUBMISSION.

| DEVELOPMENT STAGE | TIME FRAMES | PROPOSED START DATES |
|---|---|---|
| Specifications and design | 4–6 months | – |
| Approvals | 6–12 months | – |
| Tender and negotiation | 4–6 months | – |
| Construction | 42 months | – |
| Pre–opening | 3 months | – |
| Opening of the hotel | – | 2018 |
| Opening of the VIP gaming facilities | – | November 2019 |

  - $30 for Baccarat, $20 for Blackjack and $25 for Roulette (minimum total of all bets placed per player per spin). These rates are equivalent to between $2,100 and $1,500 per hour, reflecting the speed at which the croupier conducts the games; and
  - the lowest minimum bet for the equivalent game located in any of the VIP gaming areas at Crown Melbourne;
- Permitted gaming table types will include traditional table games, semi–automated table games and fully–automated table games;
- Poker machines will not be permitted;
- VIP gaming may be conducted 24 hours a day, 7 days a week, 365 days a year;
- The Crown Sydney Hotel Resort will be licensed to serve alcohol in all areas;
- Smoking will be permitted in all VIP gaming areas, provided that Crown meets its commitments in relation to air quality;
- The term of the licence should commence on 14 November 2019, and expire on the expiration date of the land lease, and
- Variations to the licence will only be made through agreement between Crown and the NSW Government – compensation would be payable to Crown if the NSW Government takes any action which has the effect of amending the key terms of the licence or has some other material adverse impacts on the operation of the hotel resort without Crown's approval.
- Crown requests that the licence be granted immediately following the enactment of new legislation and determination of suitability by the Independent Liquor and Gaming Authority (ILGA).

In addition, Crown requests certainty in relation to cost of holding this licence. Crown has proposed an upfront licence fee of either $100million or $250million, depending on the tax rates applied to VIP gaming revenue (Options A or B). Crown proposes that the upfront licence fee be payable upon issue of the licence. Crown anticipates that the licence would be issued in calendar year 2013.

### Crown seeks certainty on land access issues

Through its EDA with Lend Lease, Crown has secured the rights to negotiate and develop the proposed hotel resort within the Barangaroo precinct. Lend Lease acquired the overall right to develop Barangaroo through an earlier public tender.

There is a range of complex matters that Crown advises are impacting on its ability to conclude an agreement with Lend Lease and BDA to acquire a long term leasehold of its proposed site. These are explained, together with a recommended approach, in Chapter 4.

### Crown seeks certainty on tax rates for VIP gaming revenue

It is proposed that revenue from international and interstate VIPs will be taxed at a differential rate to revenue earned from local VIPs. As mentioned above, two combinations of these differential flat tax rates have been provided, varying with the amount of the gaming licence payment, as shown in Table 3.3. They are inclusive of GST.

It is noted that the NSW Government will provide Crown with a rebate of GST paid on international and interstate VIP gaming revenue, in line with practices for the Star.

TABLE 3.3: PROPOSED LICENCE FEE AND VIP GAMING TAX RATE OPTIONS
SOURCE: CROWN PROPOSAL SUMMARY, P. 5

| ELEMENT | OPTION A | OPTION B |
|---|---|---|
| (A) LICENCE PAYMENT | $100 MILLION | $250 MILLION |
| (B) LOCAL VIP TAX RATE (NON–REBATE) | 27.5% | 23% |
| (C) INTERNATIONAL/INTERSTATE VIP TAX RATE (REBATE) | 10% | 10% |

Crown also requests that these tax rates be appropriately adjusted in the event of any increase in the rate of GST. Crown requests the right to compensation if the NSW Treasurer was to exercise his/her power to unilaterally vary these tax rates within 30 years of issuance of the gaming licence. It is also noted that some of these proposed rates are inconsistent with the current tax structure that applies to gaming revenues of The Star.

### Crown requests an exemption from anti–smoking legislation

Crown requests that the NSW Government exempt the VIP gaming facilities from anti–smoking legislation over the long term.

Crown claims that such an exemption is essential for maintaining the international competitiveness of the facilities, particularly in relation to Asian guests. Crown will create non–smoking areas to match demand as customer preferences change.

## 3.2 CROWN'S PROPOSED COMMITMENTS

Crown proposes to formally commit to the delivery and maintenance of an iconic, 6 star hotel resort, air quality technology and responsible gaming programs.

### The hotel resort will exceed the Forbes 5–star and Australian 5–star hotel standards

Crown has defined this 6 star standard in terms of the features listed in Table 3.4 opposite.

### Crown proposes responsible gaming programs, including voluntary exclusion

As a continuance of its approach in Melbourne and Perth, Crown has proposed to establish a Responsible Gaming Support Centre, which would offer programs, services and information to staff and patrons to help minimise the incidence of problem gambling behaviour. Crown proposes to commit to a standard of care no less than is provided at Crown Melbourne. A Memorandum of Understanding has been signed with Mission Australia in relation to the provision of these programs.

This will include a self–exclusion program, which allows members to ban themselves from entering or remaining within gaming areas. If such individuals are found in breach of this voluntary exclusion, a staff member will approach them to discuss their reasons and provide information on available support services.

Crown also proposes that staff will attempt to encourage customers to utilise appropriate responsible gaming services if concerns regarding their gaming behaviour are raised with Crown by family or friends.

TABLE 3.4: CROWN'S PROPOSED 6 STAR STANDARD
SOURCE: CROWN VOLUME 1A – PROJECT SUBMISSION, P. 32

| FACILITY | 6 STAR STANDARD |
|---|---|
| **Hotel suite/villa room size** | 100—500 $m^2$ |
| **Standard room size** | 55—70 $m^2$ |
| **Lobby area** | Architecturally dramatic space with high levels of service and amenity |
| **Porte cochere** | Statement arrival with personalised greeting and capacity for limousine and valet service |
| **Facilities** | Large-scale spa facilities with segregated VIP treatment rooms and customised treatments |
| **Restaurants** | Multiple signature dining experiences with celebrity chefs in highly designed environments |
| **Restaurant covers** | Signature restaurant clustering creates a dining precinct which results in visitation<br><br>Restaurant covers are expected to be 150–200% of room count |
| **Cocktail lounge/bar** | Signature lounge environment which is 'destinational' in nature and leverages the unique aspects of the location |
| **Meeting space** | Meeting and convention space with unique outdoor environments which leverage Sydney's climate and harbour environment |

## 3.3 KEY PROPOSED FINANCIAL DETAILS

TABLE 3.5 BELOW SUMMARISES THE FINANCIAL PROPOSAL AS PUT FORWARD BY CROWN
SOURCES: DELOITTE ACCESS ECONOMIC ANALYSIS, CROWN FINANCIAL SUBMISSION

## CROWN FINANCIAL PROPOSAL SUMMARY

| FINANCIAL METRIC | RESULT |
|---|---|
| Total Capital Investment | $1,300m |
| Licence Fee | $100m (Option A)<br>$250m (Option B |
| Project (Internal Rate of Return) | Circa [redacted]% |
| NPV to Crown | [redacted] (Option A)<br>(Option B) |
| **KEY ASSUMPTIONS** | |
| Theoretical Win Rate | 1.35% |
| Melbourne Local VIP Market Growth Rate | 2013: [redacted]<br>2014—2030 : [redacted] p.a<br>2031—2038 : [redacted] p.a<br>2039 —2048: [redacted] %p.a<br>2049+ [redacted] p.a |
| Sydney Local VIP Market Size vs Melbourne | [redacted] |
| Crown Local VIP Market Share | Existing Market [redacted]<br>Incremental Market [redacted] |
| Melbourne Interstate VIP Market Growth Rate | 2013—2030: [redacted] p.a<br>2031—2038: [redacted] p.a<br>2039 — 2048 : [redacted] p.a<br>2049+ [redacted] pa. |

| FINANCIAL METRIC | RESULT |
|---|---|
| Sydney Interstate VIP Market Size vs Melbourne | [redacted] |
| Crown Interstate VIP Market Share | Existing Market [redacted]<br>Incremental Market [redacted] |
| Melbourne International VIP Market Growth Rate | 2013: [redacted] %pa<br>2014—2030: [redacted] a<br>2031—2038: [redacted] pa<br>2039+ [redacted] %pa |
| Sydney International VIP Market Size vs Melbourne | [redacted] |
| Crown International VIP Market Share | Existing Market [redacted]<br>Incremental Market [redacted] |
| Apartment Sale Revenue share (cost $200m) | [redacted] |

## PROPOSED STATE GAMING TAX RATES

| | |
|---|---|
| Local VIP Gaming (prior to RGL of 2% and GST of 9.09%) | 16.41% (Option A)<br>11.91% (Option B) |
| Interstate Rebate Gaming (includes GST) | 10.0% (Option A)<br>9.0% (Option B) |
| International Rebate Gaming (includes GST) | 10.0% (Option A)<br>9.0% (Option B) |

# 4 ASSESSMENT OF CROWN PROPOSAL

This section provides an assessment of Crown's proposal in accordance with the Guidelines for Unsolicited Proposals.

## 4.1 ASSESSMENT METHODOLOGY

The assessment applies the seven criteria in the Unsolicited Proposals Guidelines to the proposal. The approach to each criterion is as follows:

- The proposal cannot proceed to stage 3 unless:
  - Uniqueness justifies direct dealing
  - The proponent demonstrates sufficient capacity and capability to deliver the project, and
  - The project is affordable for Government

- Performance against the value to government criteria has focussed on analysis of:
  - The net economic benefit to the NSW economy, quantified as addition to Gross State Product
  - The present value of additional licence fee and taxation revenue to the State, expressed as net present value, and
  - Other benefits that cannot be readily quantified. These are described so that they can be taken into account.

- Whole of government impact assessment has focussed on potential social impacts of problem gambling, and the wider opportunity costs for future competition and casino gaming policy options. Impacts on the surrounding precincts are also considered.

- Appropriateness of return analysis has considered whether the Government, on behalf of taxpayers, would receive a fair share of returns from the project.

- Risk allocation analysis considers what risks are proposed for Government, and whether risk is assigned to the party best placed to hold it.

Once all criteria have been applied, an overall conclusion is presented. Key residual matters are then also highlighted, with proposed approaches to resolution.

## 4.2 UNIQUENESS

Unsolicited proposals are required to demonstrate unique elements. These may include characteristics such as:

- Intellectual property or genuinely innovative ideas
- Ownership of real property
- Ownership of software or technology offering a unique benefit
- Unique financial arrangements
- Unique ability to deliver a strategic outcome, or
- Other demonstrably unique elements.

### Crown holds the exclusive right to develop a hotel resort at Barangaroo South

Barangaroo South is a globally significant urban redevelopment precinct, and hence a high priority for NSW. The right to develop the land and acquire 99 year leases for a mix of office, hotel, residential and other purposes was awarded to Lend Lease through public tender. Crown Ltd has entered a contract with Lend Lease that gives it a renewable two year exclusive right to develop a hotel building on Barangaroo South. Hence, Crown has a unique asset which justifies direct dealing.

The uniqueness of this component of the project will remain the case for the term of the EDA between Crown and Lend Lease, which establishes Crown's sole right to negotiate and develop the site.

### The iconic design of the Crown Sydney hotel resort is unique benefit of the proposal

As described in Chapter 1, Crown proposes to develop a luxury 6 star hotel resort with VIP gaming facilities. At the core, the ability to build a hotel, with or without gaming facilities, which will serve to attract tourists is not unique. It is not uncommon for hotels and resorts to provide pool, spa, restaurant, bar and shopping facilities.

However, Crown proposes that the design of the building will achieve the status of a contemporary and iconic landmark. A number of key design objectives have been identified, as listed in the proposal. Overall, Crown requires that the design is

innovative, sustainable and complementary to the surrounding area of Barangaroo and Sydney more generally.

To achieve this, Crown held an international design competition, obtaining entries from three leading architecture firms in Europe and the US. The winning design, by Wilkinson Eyre, was announced on 16 May 2013.

The jury that made this decision comprised of two executives each from Crown, Lend Lease and the government's Barangaroo Delivery Authority, as well an independent architect, Roger Poole. Wilkinson Eyre has since been engaged by Crown as the principal architect for the development.

To ensure that an iconic design is met in a manner that is complementary to the surrounding area, it is recommended that the Government makes explicit reference to appropriate design criteria in the event of any approval.

## 4.3 VALUE TO GOVERNMENT

### Growth in tax and fee revenue of $441 million or $459 million

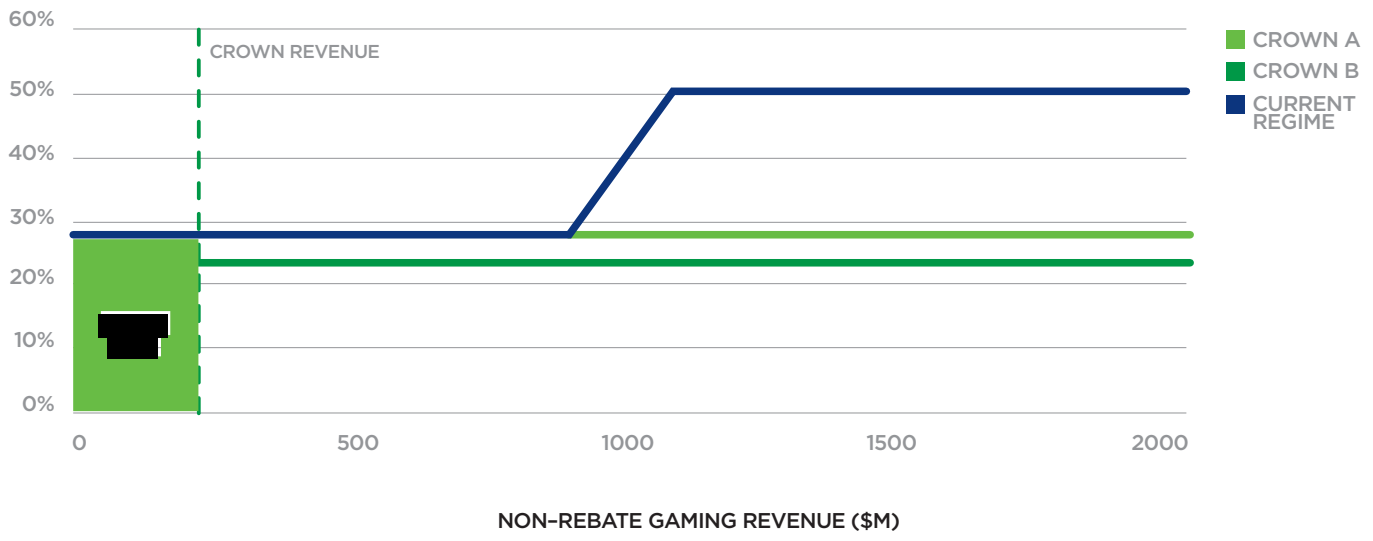
Figure 4.1 indicates Crown's proposed tax rates for non–rebate play, compared to the current regime. The revenue data is as projected by Crown for FY 2025. This analysis presumes The Star's existing tax regime extends beyond the expiry of its exclusivity.

The existing tax rate at The Star for rebate based play is 10%. The Star's non–rebate based revenue is taxed at progressively higher rates which rise in 1% increments in marginal Tax Rate for each additional $5 m of tax revenue (Tax Bands), for FY 2013 the lower threshold is $674 million taxed at 27.5%. Any remainder above this amount is taxed at increasing marginal rates that peak at 50%. The Tax Bands are annually indexed to CPI.

Under Option A with a rate of 27.5%, tax revenue for non–rebate players in 2025 is forecast to be [redacted] million.

Deloitte estimates that the NPV to FY 2035 of additional licence fees and tax payments to the State from Crown would be $441 million for Option A and $459 million for Option B. These amounts are lower than proposed in Crown's submission, as Deloitte believes that Crown's modelling makes an unduly low assumption about growth at The Star. Deloitte has also undertaken

FIGURE 4.1 CROWN'S PROPOSED TAX RATES FOR NON–REBATE PLAY



sensitivity assessments on the potential impacts on total tax receipts, should Crown's growth rely on transferring business from The Star, rather than attracting new additional business.

Under Option A, the tax rates on rebate business are the same, so transfers of business would have no tax revenue consequence for the State. Under Option B, there would be a 1% differential, which does create a risk of loss of revenue if Crown could not stimulate growth. This is not considered to be a substantial risk from a revenue perspective, but as rebate business is the principal growth opportunity, competitive neutrality would be preferable.

Crown's anticipated revenue in the non-rebate segment would not reach the threshold at which the base rate escalates in the foreseeable future. There is potential for revenue loss if the amount of non-rebate business transferred from The Star to Crown was large compared to overall growth. However, it is estimated that The Star's average tax rate on non-rebate play will be approximately 20% (excluding GST and RGL) by the time that Crown would commence operations.

Crown presents a case showing that an absolute reduction in revenue is very unlikely, and offers two guarantees to protect the State's revenue.

Under both options A and B, Crown offers to guarantee that in its first three years of operation (FY2020–22), the State will receive at least the same normalised total gaming revenue as it receives from The Star in FY2019. Normalisation is understood to provide for adjustment based on using a win rate of 1.35% and application to the Star of a base rate of 18.41% (excluding GST) for non–rebate revenue. On this basis, revenue would need to fall by 15% for the guarantee to operate.

Under option B only, Crown offers an additional guarantee that it will pay total gaming tax payments of $1billion to the State over the first 15 years of full operation (FY2022-36). For this tax guarantee to become effective, it is estimated that gaming taxes to the State would need to fall well below forecast to trigger this guarantee. Given the duration and structure of this guarantee concept, care is required to document an effective guarantee.

Although Option B offers a larger up front licence fee payment and a longer term tax guarantee, the assessment concludes that Option A provides the best value for NSW if Crown is approved to progress to Stage 3. This is because:

- It offers a greater revenue upside to taxpayers if Crown Sydney is a successful development
- It eliminates the risk of revenue cannibalisation in the rebate play segment, which is anticipated to be the major growth sector in coming years, and
- It reduces the risk of revenue cannibalisation in the non–rebate sector.

## Material costs to government

The proposal states that the development will not impose any material costs for the NSW Government.

The Government would incur additional costs of ongoing regulation of gaming, which should be recovered from Crown.

The Government will experience modest additional costs for negotiation in Stage 3, preparation of any necessary legislation and subsequent licensing. These would be small compared to the proposed licence fee and taxes.

## An iconic building can attract additional tourism

Crown's proposal presents evidence that significant growth is taking place in the Asian outbound travel market, particularly from China. It claims that the hotel resort development will help to reverse Australia's declining market share of international tourists, as well as NSW's falling national share.

The Crown Sydney Hotel Resort proposes to attract high net worth Chinese tourists, through the provision of high-quality accommodation alongside restaurant, bar, shopping and gaming facilities located within the CBD. Crown expects to grow Australia's share of the international VIP gaming market.

The Assessment Panel agrees that the Crown proposal will be an asset for Sydney but there is no third party evidence to provide an indication of how much incremental tourism will be generated directly by the hotel/casino.

## Enhanced training opportunities

Section 3 describes the training colleges and programs that Crown proposes to establish in conjunction with the Penrith Panthers Group and National Centre of Indigenous Excellence. These arrangements appear to be valuable for NSW. Given Crown's experience in Melbourne and Perth, it is likely that these activities will be undertaken voluntarily. Therefore, the Government should not request an official commitment should the proposal proceed to Stage 3.

## Assistance to local charities and community organisations represents further value to the NSW community

The proposal recognises the potential for the hotel resort to provide assistance to charities and community organisations, in a similar manner to the contributions made by Crown Melbourne and Crown Perth.

The nature of assistance which might be provided is varied,

including donations and sponsorships, provision of function rooms at a reduced price, and support through volunteer efforts of employees.

This represents further value to the NSW community.

## 4.4 WHOLE OF GOVERNMENT IMPACT

The key impacts of Crown's proposal on the NSW Government and the State as a whole are potential social impacts and opportunity costs.

The social impacts of the proposed gaming facilities are dependent on the nature of the facilities, conditions for entry, responsible gaming programs and smoking legislation.

### Crown estimates that only [redacted] of local patrons will participate in the type of gaming at its proposed Crown facility

It is proposed that the casino component of the development will comprise private gaming rooms and luxury gaming salons. There will be no poker machines or low limit tables. Crown requests approval to operate an unlimited number of traditional table games and semi-automated and fully-automated versions of those table games within the defined gaming areas.

Crown claims that a suite of restrictions, in addition to the members–only requirement will significantly limit the risk of problem gambling behaviour. Specifically, Crown estimates that approximately [redacted] of local gaming patrons would be attracted to the proposed VIP gaming facilities, based on Crown Melbourne data. The minimum annual turnover per local gaming patron at the proposed Crown Sydney Hotel Resort is estimated by Crown to be between [redacted] and [redacted] The revenue to Crown depends upon the game played and actual win rate of the patron.

For regulatory purposes, it is necessary to define a 'gaming site' should the development be approved. Crown proposes that this definition should take the form of a limit on the total floor space occupied by table games, being the lesser of:

- 20,000 $m^2$ or
- 20% of the final approved total gross floor area of the building.

The proposal also provides a definition for low limit tables. Low level tables mean a minimum bet limit of less than the lower of:

- $30 for Baccarat, $20 for Blackjack and $25 for Roulette (minimum total of all bets placed per player per spin). These rates are equivalent to a turnover per hour of between $2,100 and $1,500.; or
- the lowest minimum bet for the equivalent game located in any of the VIP gaming areas at Crown Melbourne from time to time.

The Assessment Panel recommends that the limits should be the higher of these two levels. In addition, the licence should include conditions to control the types of games that may be played, namely:

- Games that may be conducted by a croupier are restricted to games approved by the regulator; and
- Automatic or semi–automatic table games may only be used to play games approved by the regulator, and which are conducted simultaneously by a croupier in the facility.

### Entry to the VIP gaming facility will be restricted to members

Crown's proposal states that entry to the VIP gaming facilities at the hotel resort will be restricted to members, from either local, interstate or international segments. These members will be permitted to attend the facilities in the company of a limited number of guests, who will also be permitted to participate in table games.

According to the proposal, prospective members would be required to complete an application form and acknowledge that they are aware that they are requesting to join a VIP gaming facility subject to the licence conditions that are described above and in Section 3.

Crown proposes to review memberships on a regular basis, paying particular attention to playing history. Members with a history that is inconsistent with a VIP gaming facility may not be entitled to membership renewal. Crown also proposes to examine whether individuals are members of VIP gaming facilities within Australia or overseas.

Crown claims that the provision of access to the general public is not in its commercial interests, as this would have a significant impact on the proposed exclusivity and private nature of the facility.

This clear incentive is acknowledged. However, a concern remains regarding the likely strength of this incentive during times when Crown may be unable to attract sufficient VIP members to fully utilise the facilities. Additional measures to complete the definition of VIP gaming are included in the recommendations of this report.

### Crown has proposed to implement responsible gaming programs

Crown's responsible gaming programs are described above. It is recommended that the ongoing delivery of responsible gaming programs be specified as a requirement for the development. This should define mandatory ongoing programs, an initial suite of campaign programs that might be adapted over time, and include a minimum level of commitment to such programs. Voluntary self–exclusion should fall within the mandatory ongoing programs category.

Crown proposes that if it receives notice of concern from a family member or friend of a member in relation to their gaming behaviour, staff will seek permission to approach and discuss those concerns with the individual. A commitment to develop third party exclusion procedures to protect families should be included in a final binding offer.

### Crown proposes to install and monitor state–of–the–art air quality technology

The final core social impact that should be considered is the need for changes to NSW smoking legislation. Crown claims that the provision of VIP smoking exemptions will be critical to the international competitiveness of the hotel resort, and gaming facilities more specifically, particularly in relation to the Asian tourist market.

The proposal notes that similar exemptions from smoking laws are provided for all existing major VIP gaming areas within Australia (including The Star), consistent with allowances in Singapore, Macau, Philippines and Las Vegas. Crown seeks a long term exemption as part of the conditions for its VIP gaming licence.

To protect health, Crown proposes to install state–of–the–art air quality technology with monitoring to be undertaken on a quarterly basis by an independent expert. The results of this testing will be made available to the NSW Government in the form of compliance reports, as well as the health and safety representatives of affected Crown employees. An annual report will also be provided to the Government.

The proposal notes that Crown may set aside some non–smoking tables within the VIP gaming facility, in accordance with the evolving preferences of its customers.

The Assessment Panel recommends that anti–smoking exemptions be provided to Crown for the purposes of the gaming facility. This is justified on the basis that it will maintain consistency with other jurisdictions and allow the venue to compete on an international platform. It is recommended that a final bid should include provisions that require Crown to negotiate periodically in good faith to reduce or remove smoking exemptions in line with the practices of the majority of its competitors at the time.

### The Opportunity Cost

NSW currently has only one casino. The operator, Echo Entertainment Ltd has proposed to pay $250million over 19 years to the Government if it agrees to renew the exclusivity of its licence. The present value of this payment is estimated at $157m. This is the direct opportunity cost should the Government agree to progress Crown's proposal.

As Crown does not seek exclusivity for its licence, accepting its proposal would not remove future gaming policy options, should government decide to pursue new market models in the future.

## 4.5 APPROPRIATENESS OF RETURN ON INVESTMENT

The Crown proposal has been assessed against the criteria of appropriateness of the return on investment (ROI).

### Approach to estimated return on investment

This measure has been estimated by Crown, given the risk of the project.

The key elements of the analysis of the appropriateness of the return are:

- Comparison with returns on precedent transactions within NSW, and
- Comparison with returns achieved by companies operating in similar industries.

### Crown's financial model has been analysed

The Crown financial model calculates the costs and revenues associated with the development of Crown Sydney over a 99 year term. Revenues are calculated based on an assumption of the potential size of the Sydney market compared to the Melbourne market, along with forecasts of growth rates in each segment (local / interstate / international). Costs are generally set out as a proportion of revenue or as individual assumptions based on experience at Crown Melbourne.

The following issues have been identified when examining the return calculations:

- The financial model provides an analysis based on the weighted average cost of capital for Crown. If the gearing level within the Crown corporate entity is applied, then the reported return on equity of the investment should be higher. Care must be taken when reviewing the

appropriateness of the returns that the appropriate return measure is being used.
- Given the high sensitivity of returns to net revenue, the flat rate of tax as proposed by Crown may result in returns that are higher than modelled.

The Assessment Panel has undertaken a sensitivity analysis in order to understand the relative impact of varying different assumptions in the financial model. The analysis has been conducted based on the tax regime included in the Crown model.

The analysis shows that the critical assumptions relate to the revenue for the project are win rate and market growth rates.

These impact on both the returns to Crown and the tax revenue.

## APPROPRIATENESS OF RETURN ON INVESTMENT

The Crown proposal has been assessed against the criteria of appropriateness of the return on investment. The Assessment has evaluated commercial-in-confidence data that has been provided and concludes that the Crown Unsolicited Proposal return is consistent with comparable projects. For the Crown Melbourne expansion phase (2008-12), Crown indicates that it invested [redacted] and has achieved incremental EBITDA of [redacted] a current return on this metric of [redacted]

### Comparable Companies

Table 4.2 below sets out the Return on Equity (ROE) and Return on Assets (ROA) for comparable companies in the gaming industry provided by recent equity market research reports. It should be noted that lower returns are normal for an established company than for a new business where there are additional risks around development/construction of the facilities and uncertainty over the level of revenue that the new facility will generate.

TABLE 4.2: COMPANY RATES OF RETURN COMPARISON

| COMPANY | ROE | ROA |
|---|---|---|
| AUSTRALIAN | | |
| **Echo Entertainment Ltd** | 2.4%[redacted]<br>4.3%[redacted]<br>5%[redacted] | 1.5%[redacted]<br>5.8%[redacted]<br>6%[redacted] |
| **Crown Ltd** | 14.1%[redacted]<br>16.3%[redacted]<br>14.1%[redacted] | 8.5%[redacted]<br>9.5%[redacted]<br>11.7%[redacted] |
| INTERNATIONAL | | |
| **Las Vegas Sands**<br>**Wynn Resorts**<br>**Penn National Gaming** | 20.9%[redacted]<br>54.9%[redacted]<br>11.6%[redacted] | 6.9%[redacted]<br>7.1%[redacted] |

With reference to the above U.S. based gaming companies, care should be used with any comparisons to Australian gaming companies due to their significant use of debt in their capital structures. U.S. companies run with debt/EBITDA in ranges of 2.5-8x, compared with Crown's average over the past few years of under 2x. The Crown Unsolicited Proposal return is deemed appropriate for the proposal and for Crown.

### BROKER ESTIMATES OF RETURNS

Several brokers have estimated the likely returns to Crown for its investment in Barangaroo if the project were to go ahead. These provide an estimate of the market's view of the required returns for the project.

- In a May 2013 report, [redacted] estimates that the project IRR would be circa 9.7%
- In a June 2013 report, [redacted] estimates that the required return for the project would be about 10%

Indicative project returns for the company are considered not excessive.

## 4.6 CAPABILITY AND CAPACITY

The Crown proposal has been assessed against the criteria of capability and capacity.

After reviewing Crown's proposal, the following issues have been identified as central to Crown's capability and capacity. They are examined in turn in this section.

- Exclusive right to plan and develop the land site; and
- Crown Limited's financial position.

### Right to develop the site

Through its EDA with Lend Lease, Crown has secured the rights to negotiate and develop the proposed hotel resort within Barangaroo South. [redacted] Lend Lease is currently in a legal dispute with the BDA over the calculation of 'value share' payments, and Crown believes that this is impacting on its ability to finalise an agreement with Lend Lease.

'Value share' payments are part of the consideration payable by Lend Lease to BDA for the rights it obtained under the Project Development Agreement for Barangaroo South. Under that agreement, Lend Lease pays BDA both a fixed amount for land, and also variable 'Value Share' Payments. Value Share Payments are calculated by reference to the unimproved value of the land, and the valuation process under the Project Development Agreement can proceed once the legal dispute is finalised.

Crown has proposed that its building would remain within the methodology to be used to calculate value share, with the exception that the portion of potential value (if any) that arises from the gaming business would be excluded from the calculation. However, the value uplift (if any) of the gaming business on the rest of the building would be captured within the value share methodology that would continue to apply to the rest of the building. The gaming business value would be captured within Crown's proposal licence fee.

This is proposed because there is circularity in the methodologies – calculation of value share requires knowing the value of the licence, however, valuation of the licence requires knowledge of any value share liability.

The assessment supports Crown's approach, because in its absence Crown would be likely to make a provision for a potential value share liability, and thus reduce the amount it would pay for the licence. It is also likely to be complex to insert a prospective value for a gaming business into a methodology that was designed for more conventional buildings such as offices, apartments and hotels. The proposed approach would maximise the likely licence fee, and bring forward its receipt. This approach will, however, require the agreement of Lend Lease and BDA. The risk of failure to obtain such an agreement should remain with Crown.

Crown has also proposed its gaming areas should be excluded from the methodology that applies for measuring the environmental and sustainability performance of the overall precinct. The Assessment Panel recommends that Crown's proposed alternative, which is to implement the world's best practice that is available for VIP style gaming facilities, should be adopted. It is understood that the material factor is the exceptional energy costs required for lighting and for special air conditioning in areas where smoking is permitted.

### Crown's financial position

In order to undertake the development, Crown will be required to finance the $1.3billion in capital costs plus licence fees. In this section Crown's financial capacity to undertake this investment based on its current financial position is discussed.

The proposal refers to Crown's established financial position as an indicator of its capability and capacity to deliver. In particular, it highlights the following strengths:

- Crown is an S&P / ASX 50 company with a market capitalisation of circa $9billion;
- As reported for the half–year to 31 December 2012: weighted average maturity of drawn debt of 5 years, and undrawn bank facilities of $772 million. As advised to the market on 22 February 2013, Crown's debt maturity profile is notable with long duration and over $900 million

maturing beyond FY2020;
- Investment grade BBB flat, stable outlook, credit ratings from S&P, Moody's and Fitch; and
- Strong, consistent revenue and EBITDA growth for Crown Melbourne and Crown Perth since acquisition. Further capital expenditures in Burswood Casino are tapering off and accordingly this frees up operating cash flow and debt capacity to support the proposal.
- Crown is an experienced borrower in the bank markets with longstanding and wide bank support. Additionally, Crown is experienced in both the U.S. and Australian debt capital markets. With recent debt capital markets issues during 2012 (A$300million 5 year bonds, A$532million subordinated notes), Crown's debt maturity profile for upcoming years is expected to show diversity of sources of borrowings and a manageable maturity profile. Crown's public disclosure of its Key Financial Ratios indicates that it has ample headroom to absorb any adverse conditions with its existing operations and to support the proposal. Crown is very experienced and respected for its capital management strategies.

This financial strength is acknowledged. In the 2011-2012 financial year Crown Limited posted a normalised net profit of $415million after tax, a 22% increase on the previous year's results. Crown also reported an operating cash flow of $571million over the course of the year. The equivalent figure for 2010-11 was $451million. Meanwhile, in line with Crown's capital expenditure projects in Melbourne and Perth, total outstanding debt has increased, from a total of $1,069million in 2010-11, to $1,694million in 2011-12, and reported $1,942million at 31 December 2013. This is expected to reduce as the projects wind down. In addition, the recent sale of the 10% holding in Echo Entertainment has released approximately $260million of cash that can be redirected to investments such as the Crown Sydney proposal.

Overall, it is the Assessment Panel's view that Crown's capable financial management and current financial position is strong enough to support the capital expenditures and risks associated with the proposed development, particularly as the proposed capital expenditures would be staged over the period from FY2014-2018. In this regard, it has the capability and capacity to implement the proposal.

### Crown has a track record in the tourism industry

Crown's experience in the tourism industry also reinforces its capability and capacity to deliver the proposed development. This section acknowledges Crown's strengths in relation to its:
- Experience in design, construction and operation of hotels and gaming facilities;
- Experience in the tourism industry;
- Experience in staff training and development;
- Ability to utilise industry partnerships; and
- Ability to deliver broader social benefits.

Crown's experience in designing, constructing and operating hotels and gaming facilities in Australia and overseas is not disputed. In particular, the success of investments at Crown Melbourne and Crown Perth enhance Crown's capacity to develop and operate the proposed hotel resort. The experience and consistency of the company's board and management team is also an important contributor in this regard.

In relation to design, the likely benefits of the international design competition are recognised. However, it is noted that the concept of what is 'iconic' building architecture should be defined if the proposal proceeds to Stage 3. Although issues of design are highly subjective, measures should be put in place to ensure that the hotel resort will indeed complement the surrounding area at Barangaroo. BDA is best placed to lead this, together with the Department of Planning and Infrastructure. Crown's credentials for the responsible service of gaming are also acknowledged. It is expected that this record will continue should the Sydney hotel resort receive approval.

Finally, Crown's record in relation to probity and compliance with legislation and internal controls has been noted.

Crown refers to its experience in attracting VIP tourists to its facilities in Melbourne and Perth. In part, it credits its success to its high quality service offering, valuable assets and brand recognition. This is acknowledged. While it is accepted that Crown is capable of attracting high–yielding tourists, it is important to also consider whether other providers, with a broader global presence, would exceed Crown's performance in this regard. Crown's ability to provide access to the Ellerston Day Retreat and the Perisher Ski Resort is noted as an addition to its offering.

Crown is a major Australian employer, with extensive experience in the provision of training programs and development opportunities for its staff. Given this experience, Crown is considered to be more than capable of delivering additional training colleges and courses relevant to the proposed hotel resort.

Crown's proposal is strengthened by partnerships with the NCIE, Penrith Panthers Group and United Voice. These are expected to significantly improve Crown's capacity to deliver on its employment and training objectives, particularly in relation to Indigenous employees, workplace rights and development of pathways from schools and TAFEs to employment opportunities.

At present, each of these partnerships has not proceeded beyond the stage of a Memorandum of Understanding. It is therefore uncertain whether these will advance to formal contractual agreements, and if so, what form these agreements would take.

Regardless, it is not apparent that these partnerships are critical to Crown's capability and capacity to deliver. While there is no doubt that they would strengthen Crown's position, the

achievement of formal partnerships should not be required as a commitment for Stage 3.

Crown has also indicated that it will provide employment for people with disabilities, support local charities and community organisations, and implement measures to reduce the impact of the hotel resort on the environment. Crown's capability and capacity to achieve these objectives is noted, given the credentials of Crown Melbourne and Crown Perth.

## 4.7 AFFORDABILITY

There are minimal costs for government during the construction or operation phases of the proposed development.

The proposal states that the NSW Government will not be required to contribute any funding towards the construction of the hotel resort.

However, it is likely that costs will be incurred by the Barangaroo Delivery Authority (BDA) as it oversees the development process. However, these costs are not unique to this proposal.

Similar costs would arise for any alternative development at the site.

The costs contemplated in this section are minor when compared to the economic and tax receipt benefits to NSW outlined in the Crown proposal.

There will be additional costs, for example those associated with negotiating Stage 3 and (if approved) drafting and passing appropriate legislation.

### Costs for Government during operation

The proposal also acknowledges that, should the gaming licence be approved, NSW Government gaming regulator would require additional resources to carry out its regulatory role for the VIP casino. These should be recovered from Crown each year.

## 4.8 RISK ALLOCATION

### The risks to NSW Government are low

The risk allocation proposed by Crown is set out in the Table 4.3 opposite.

### Direct risk of investment

According to Crown's proposal, the NSW Government will not bear any substantial risk associated with the project, apart from actions that are within NSW Government's control that are required to allow the project to proceed (for example granting a casino license and fulfilling obligations under the Barangaroo Project Development Agreement with Lend Lease to make the site available). The majority of the risk of the project will be taken on by Crown.

Under Crown's proposal, Government will take risk on the level of gaming tax revenue received from Crown. However, as tax revenue is calculated from Crown's gaming revenue, there will be incentive for Crown to maximise the level of tax to the State in order to maximise their returns from the investment. Crown describes the financial worst case scenario for government as the case where the hotel resort does not reach its proposed revenue targets. In that case, NSW would continue to benefit from the 6 star hotel, and receive tax revenue from the gaming facility. Crown has also proposed two tax guarantees which are discussed above.

### Consideration of regulatory risk

Crown has requested formal confirmation from the NSW Government that it will not make changes to the regulatory environment within which the hotel resort will operate without agreement from Crown. This encapsulates:

- Changes to the tax regime
- Changes to licence payments
- Changes to the regulatory regime which materially adversely impact the financial operations of the hotel resort, and
- Changes to the smoking exemption in the VIP gaming areas.

The Assessment Panel acknowledges Crown's need for regulatory certainty for a defined period before commencing the development. It is therefore reasonable that compensation from the NSW Government may be payable to Crown in the case that changes in clearly specified regulatory areas are made within an agreed framework of scheduled periodic review. This is the approach that currently operates at The Star.

The assessment recommends that the tax rates and the licence fee should be reviewed after 20 years. Certain matters, such as licence duration and location are matters that should not be subject to unilateral change. Other fundamental entitlements to conduct casino games, smoking exemption, 24 hours of operation are matters that need to be agreed. The premise is that there shouldn't be any erosion of ILGA's current powers, however the Government and ILGA should consider a review of the regulatory environment in view of competitive neutrality and greater regulatory efficiency. The details of these matters should be resolved in Stage 3.

TABLE 4.3: RISK ALLOCATION PROPOSED BY CROWN

| RISK | ALLOCATION |
|---|---|
| **SCOPE AND SPECIFICATION RISK** | |
| Scope/specification risk | Crown |
| **SITE AND APPROVALS RISKS** | |
| Site availability and access risk | Crown (also Government through BDA) |
| Site condition risk | Crown & Lend Lease |
| Land acquisition risk | Crown, Lend Lease & Government |
| Environmental approvals risk | Crown |
| Planning approvals risk | Crown |
| Gaming licensing | Government |
| Design, construction and commissioning risks | Crown |
| Design risks | Crown |
| Construction risks | Crown |
| Construction cost escalation risk | Crown |
| Supplier risk | Crown |
| Initial staff sourcing | Crown |
| Initial staff training | Crown |
| Facility commissioning | Crown |

| RISK | ALLOCATION |
|---|---|
| **OPERATING RISKS** | |
| Demand Risk | Crown<br>(Government indirectly through link to tax payments) |
| Win Rate Risk | Crown<br>(Government indirectly through link to tax payments) |
| Operating performance risks | Crown |
| Maintenance risks | Crown |
| Operating cost escalation risks | Crown |
| Obsolescence risk | Crown |
| Competition risk | Market participants |
| **OTHER RISKS** | |
| Interface risks | Crown, Lend Lease and Government<br>(over development issues) |
| Change in legislation/regulation risk | Government<br>(through reimbursement mechanism) |
| Legal risk | Government to review compliance<br>with existing documents |
| Tax revenue risk | Consistent tax rates and tax guarantees<br>to minimise Government risk |
| Industrial relations risk | Crown |

# 5 ASSESSMENT CONCLUSIONS

The Assessment Panel has compared Crown's two options. Option A, with a lower up front licence fee of $100million but higher ongoing tax rates is recommended because it provides the opportunity for taxpayers to receive a greater share of the upside if Crown's proposal is successful, and because it maximises competitive neutrality if The Star's tax rates are maintained at current levels when renegotiated in FY2020.

## Option A is suitable for progression to Stage 3

Crown's proposal performs satisfactorily against all the criteria specified in the Guidelines for assessment of unsolicited proposals.

Crown makes a convincing case that there is a substantial economic opportunity for NSW to benefit from the growing Asian gaming and tourism markets, and that it has the capability to deliver a large project that is likely to substantially improve NSW's share of the premium end of those markets. The project would also make a substantial contribution towards activation of the world class Barangaroo precinct. Both outcomes are priorities for the NSW Government.

Deloitte estimates that the proposal would lead to an increase of GSP of $388million by FY2022 and $442million by FY2025. Deloitte's baseline estimate of the NPV of additional licence fee and tax payments under option A would be $441million for the period to FY2035.

The entry of a competitor into the NSW casino market is expected to create an ongoing stimulus for improvement of the quality of the industry's offerings, enhancing the overall appeal of the State as a destination. As Crown does not seek exclusivity, the key opportunity cost of the Crown proposal would be potential for future exclusivity payments from Echo, including the $250 million over 19 years (NPV of approximately $157 million) that has been proposed.

Provided appropriate conditions are locked in, including a commitment to develop third party exclusion procedures to protect families, Crown's proposal is not expected to significantly increase social harm arising from problem gambling. Additional recommended conditions are presented for consideration.

These seek to increase clarity and protect the State's interests during Stage 3.

On the basis of the above, the Assessment Panel concludes that the proposal warrants progression to Stage 3 of the Unsolicited Proposals Framework, which can lead to a Final Binding Offer. If the Government accepted the Final Binding Offer, Parliament, the independent gaming regulator and planning decision-makers would then all need to consider and approve the various legislation, licences and approvals that would be required. These mechanisms would provide the opportunity for public consultation and input before the proposal could proceed.

## VIP gaming criteria

VIP gaming criteria are of critical importance to competition and determination of the appropriate licence fee. It is recommended that Crown must agree to additional measures to complete the definition of VIP gaming as a condition for entering Stage 3.

These would be as follows:

- Minimum bets for table games would be the greater of the amounts shown in Crown's proposal or those applying in its VIP areas in Melbourne ;
- Crown's proposed membership system for Crown Sydney would need to be elaborated, including a process of regular review, and a 24 hour cooling off period for new members before they commence gaming, unless they can demonstrate a VIP gaming track record;
- Third party exclusion procedures to protect families;
- Procedures that will ensure that admitted guests are bona fide; and
- Adoption of front money requirements for rebate based players consistent with NSW regulatory requirements that will apply at The Star.

## Future review of licence fee

Taxpayers should be confident that fair value has been obtained in exchange for the valuable privilege conferred by a licence. Crown has proposed a once–off licence fee for a 99 year licence.

The assessment finds that Crown's proposed licence fee and tax payments represent fair value for the reasonably foreseeable period of the licence. This is based on the relatively low rates of return indicated in Crown's financial model.

However, actual returns may prove significantly better than indicated, in which case NSW taxpayers should have the opportunity to obtain a share of anticipated uplift in the value of the licence. It is therefore recommended that as a condition of entering Stage 3, the licence fee and tax rates should be subject to review every 20 years. The review should be conducted with reference to market conditions, performance and competitiveness. Timing for the review of both casinos will be aligned.

Deloitte Access Economics

# Assessment Report Appendix

## Unsolicited Proposal from Crown Limited

July 2013

Deloitte.

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# Methodology Note

This Appendix reviews the Allen Consulting Group "Crown Sydney Proposal, An Economic Benefit Assessment" included as part of the Crown Unsolicited Proposal (UP) submission documentation. This report considers the estimated economic benefits which would arise out of:

- the Crown Sydney project; and
- an alternative hotel development project at Barangaroo South in the absence of Crown Sydney.

The difference between these two demonstrates the net economic benefit of the Crown Sydney project for NSW in terms of Gross State Product (GSP), employment, export income and taxation.

The methodology used by Allen Consulting Group to undertake this analysis is **computable general equilibrium** (CGE) modelling which seeks to quantify the economy wide effects of Crown's unsolicited proposal. A CGE model is a mathematical model of an economy that is capable of capturing economy wide impacts and inter-sectoral reallocation of resources that may result from a shock to the economy. As an analytical approach CGE modelling is useful when a direct impact, at either the specific industry or regional level, is expected to have economy-wide implications or significant 'flow-on' effects.

The CGE Model used the Monash Multi-Region Forecasting Model (MMRF). This is a multi-sector CGE model of the Australian economy that encompasses all states and territories. It was developed by the Centre of Policy Studies at Monash University.

The CGE model allows policy analysis in a single, robust, integrated economic framework. The model projects changes in macroeconomic aggregates such as GDP, employment, export volumes, investment and private consumption. At the sectoral level, detailed results such as output, exports, imports and employment are also produced.

The model is primarily based on input-output or social accounting matrices, as a means of describing how the Australian economy is linked through production, consumption, trade and investment flows. A key property of the model is that productive resources are assumed to be finite and everything must add up. In particular, spending by local visitors will not be incremental. That is, their overall entertainment budget will be unchanged, with what they spend at Crown Sydney being offset by reductions in other forms of entertainment. However, an injection of economic activity to the State from an increase in international visitors is seen to have a positive impact on GSP.

The first step for analysing an economic impact of an event in a CGE model is to establish the **base case** - what would happen in the economy in a business as usual scenario. This requires the establishment of key projections in the economy.

The second step is to develop a set of inputs to the CGE model that will 'shock' the base case and generate a new set of outputs that represents the impact on the economy of the **'policy scenario'**.

Inputs representing the Crown's Unsolicited Proposal in the Allen Consulting Group reports include:

- Capital expenditure during construction
- Operating expenditure
- Revenue generated – including hotel, gaming, food and beverage, and entertainment from interstate, interstate and international visitors
- Direct contribution to employment measured by the number of people employed both in construction and operations.

Having appropriately specified the inputs to the model, the CGE model is run to generate a series of outputs that demonstrates the impact of the 'policy scenario'.

The analysis undertaken in this Appendix concurs that the CGE modelling approach is the appropriate approach to estimate the economic impacts of the Crown Unsolicited Proposal. The analysis, however, considers the establishment of the base case.

The main consideration examined in the following analysis is the **revenue generated** in the gaming segment of the base case of Crown's proposal, that is, the expected gaming revenue generated by the current casino operation in Sydney (that is, 'The Star' owned by Echo Entertainment Group). It is considered that capital expenditure, operating expenditure, and employment inputs are all reasonable estimates.

The other main focus of this Appendix is to consider the implications for the **amount of taxation** received by the NSW Government from both the gaming revenue from the Crown Unsolicited Proposal as well as the operations at The Star.

In undertaking this analysis it is assumed that the business as usual taxation regime for The Star beyond 2019 is the current taxation regime.

# 1 Overview

The analysis provided in this Appendix reviews the economic and taxation impacts of the Crown Unsolicited Proposal (UP). The analysis is based on the information contained in the Crown final proposal lodged on 21 June 2013 as well as previous information requested around the economic modelling inputs and outputs.

The main conclusions are as follows:

## VIP Global Market - size and growth:

Deloitte Access Economics (DAE) agree that the overall size and growth of the global VIP gaming market (for both 'high rollers' and the broader market that reflects the rising Asian middle class, particularly China) is set to continue to expand solidly over the forecast period. Also, in any case, Australia represents a relatively small part of the global market. In these circumstances, there is the potential for Australia to capture a materially larger part of the global market with well-tailored offerings. The precise size of the Australian market share will depend on the quality of those offerings.

## Forecast revenue growth:

Crown's proposal does appear to have the potential to attract the global market, as demonstrated by their track record in the Melbourne market. In these circumstances, DAE accept that Crown's assessment of the potential size of the Sydney market relative to that in Melbourne (or as a share of the global market) is reasonable.

## Baseline forecast revenue growth:

Crown assumes only small real growth for the Sydney market (i.e. for The Star operations) in the absence of the Crown entering the market. DAE believe this to be unduly low based on the recent performance of The Star. We have adopted a mechanical approach which has total gaming revenues increasing in line with Treasury's projections for tax revenues to the end of the forward estimates period (6.4% p.a.) and we assume around nominal gross domestic product thereafter (5.5%).

## Economic Impacts:

Crown estimates the net impact on GSP is $566 million by FY 2022, based on its assessment of the Sydney market and an alternative 5 star hotel development at Barangaroo. Based on the above analysis, we judge that this should be adjusted for a higher baseline case. Using Crown's estimate of market size, we estimate that the impact on GSP will be $388 million by FY2022. This is our central case estimate.

This implicitly assumes that the current casino operations in Sydney, 'The Star', will not undertake further significant investments. However, it could well do so to fully exploit its remaining period of exclusivity and given the exposure to competition that would result if the Crown proposal was accepted. If The Star were to do so, the impact on overall GSP would be higher.

Crown's economic modelling does not include any additional tourism expenditure outside the casino and hotel complex. DAE have no information on the likely size of this expenditure. However, we note that there would also be some additional tourism expenditure outside the alternate 5 star hotel and, whilst they will be different types of tourists (both in numbers and spend), we assume that the net impact of this consideration on the analysis is negligible.

This analysis is subject to potential downside and upside factors which might affect the economic assessment of Crown's proposal. Potential upside factors include higher casino win rate and greater potential growth in the Australian market share of the international VIP market. Potential downside factors include lower revenue growth than forecast if Sydney is not a more successful market than Melbourne and/or stronger than expected competition from new casinos entering the market in Asian jurisdictions.

## Other Economic and Social Benefits:

Crown's proposal includes elements which may lead to other economic and social benefits, such as training colleges in Penrith and Redfern and assistance to charities and community organisations. These are not specifically quantified in the above impacts on GSP but need to be considered as part of the qualitative evaluation of the proposal.

## Taxation Impacts:

Crown proposes two tax regimes, one with higher tax rates and a lower licence fee (Option A) and the other with lower tax rates and a higher licence fee (Option B). The difference in NPV (using Treasury approved discount rates) for these options is around $48 million greater for Option B.

However, given the level of risk, the modest differences in NPV, and the implications for other tax regimes post 2019, it appears that **Option A** may generate the greatest benefits for the NSW Government. The higher tax rates presented in this option will allow the NSW Government to capture a greater share of any upside, particularly given the implications for gaming tax regimes beyond 2019.

# 2 Potential size of the market

PwC's Global Gaming Outlook 2010-2015 (released in February 2013) estimated the total global gaming market at US$147 billion and put the compound annual growth rate (CAGR) of this broad definition of gaming at 9.2% over 2010-2015 with the Asia Pacific region expected to grow the fastest at a CAGR of 18.3%.

PwC note that the growth of the casino industry in the Asia-Pacific region is being fuelled broadly by:

- The continuing economic growth and subsequent increment in disposable income of the working classes.
- The rise of a large and well-to-do middle-class.
- A long-standing cultural attachment to various forms of gambling.
- The ballooning number of new gaming venues and fresh urban centres encouraging the casino industry.

The Innovation Group estimates the size of the international VIP[1] gaming market (i.e a subset of the total gaming market) at US$33 billion in FY2012 (based on gross gaming revenue) with the largest market being Macau at US$26 billion. They also estimate that the international VIP gaming market is expected to grow at a nominal average annual growth rate of 6.7% p.a. between 2012 and 2022. Their estimate considers historical growth, the maturation of developing economies, the addition of new supply in existing markets and the opening of new markets.

Colliers International Gaming Group (CIGG) has independently provided the opinion that the above estimates of size and potential global VIP growth rates are reasonable.

Crown estimates that the international VIP market "turnover" is approximately $2.5 trillion in FY2012. They estimate that the Australian market share of this international VIP market turnover is approximately 2.5%.

From this evidence it is a reasonable assumption that the **global VIP gaming market is large and growing** in all segments, despite the addition of new supply of gaming venues and a competitive global environment.

Whether Australia can increase its share of this market above the estimated 2.5% will depend on the product offering. Evidence in other countries demonstrates that the addition of new product does drive increased gaming revenue.

For example, in the dominant market of Macau since the granting of the concessions in 2001, growth in gross gaming revenue (not VIP only gaming) has averaged about 30% per year according to CIGG. Further, growth in gross gaming revenue is expected to be in the

[1] Note that the exact definition of the 'VIP market' is not explicitly defined in the Innovation Group report but it is assumed to include high rollers (or 'whales') that are well known in the international gaming industry and receive rebates on betting turnover and other incentives (such as flights and complementary hotel suites) from casinos to attract their business.

range of 15 to 20% per annum to 2015 as a number of new casinos are planned (CIIG, PwC Global Gaming Outlook).

Singapore legalized gambling in 2005 and tendered for the construction of two casinos in 2006. Genting Singapore and Las Vegas Sands won the bids for the concession of operating the casinos. Both opened in 2010 and they have been built inside two integrated resorts in Sentosa and Marina Bay, and include attractions such as theme parks, hotels, convention centres, theatres and luxury retail shops. Growth in gross gaming revenue for the Singapore market is expected to be in the order of 20.5 % CAGR between 2010-15 (PwC Global Gaming Outlook).

CIGG advised that in the global market it is not common for jurisdictions to offer exclusive rights to casino licences. Most countries/regions have more than one casino. The only recent casino monopoly that we are aware of in Asia is Phnom Penh where Nagaworld has an exclusive within a 200 km radius of the city. In CIGG's view, monopolies are usually only granted where there is uncertainty as to the viability of a casino. This was the case in Phnom Penh, although these fears were unfounded and the government is now being pressed by other parties to break the monopoly only a few years after it was granted. In other new markets such as Singapore (as mentioned above) the government has sought a minimum of two bidders, one effectively for the CBD and one for a resort island. In Macau the removal of the monopoly ten years ago has seen a massive boom in development in the territory.

The above considerations of global market size and growth potential have been incorporated into the analysis below. It is clear from the above that the demand side of the industry is not a constraint on the potential growth of the industry in Australia, but a competitive product offering will be critical if Australia is to grow market share. The general lesson learnt from overseas experience is that a competitive market environment does not constrain market growth.

The analysis in this report makes the implicit assumption that the current casino operation in Sydney ('The Star' owned by Echo Entertainment Group ('Echo')) will not undertake further investments beyond those needed to maintain its existing facilities. Deloitte Access Economics (DAE) is not in a position to assess the nature of Echo's competitive response in the event that Crown's Proposal is accepted. However, in a competitive market where Echo's offerings are likely to continue to be differentiated from Crown's, and to fully exploit its remaining years of exclusivity, Echo may decide to continue to upgrade The Star. As such, the extent of additional competition – and its effects on market growth – is not quantified in this report.

However, it is reasonable to conclude that Sydney's ability to attract international VIP players (and, in the case of The Star, the international mass market as well) would be materially stronger if Crown and Echo were both to develop their respective offerings. This reflects:

- a degree of complementarity in the offerings with Crown targeting especially the high end of the Asian high roller market and Echo focused on providing an integrated resort product (well connected to a redeveloped convention centre facility and broader entertainment precinct) that would be attractive for a wider Asian market as well as the high roller market;

- the competitive pressure provided by some overlap in the two offerings in the international VIP space would encourage the two participants to continually innovate and refine their products (the recent examples of Macau and the revival of Las Vegas would support this thesis); and
- the fact that even if both Crown and Echo were successful with their respective offerings, Australia would still account for a small proportion of what is expected to be a growing global market.

# 3 Growth assumptions

As outlined in the methodology section, economic impacts are determined by the differential between a business as usual baseline and incremental growth as a result of the proposed investment. This chapter details Crown's proposed business as usual baseline and incremental growth and DAE's assessment of this modelling.

The market growth assumptions included in Crown's modelling are outlined in Table 3.1.

[redacted]

The outcome of these growth assumptions is shown in Chart 3.1.

**Chart 3.1: Gaming revenue assumptions – Crown's Unsolicited Proposal (UP) baseline and proposal ($m)**

[redacted]

According to Crown's model, the international rebate market currently accounts for approximately [redacted] Sydney's total casino gaming revenue. Crown expects international

rebate gaming revenue in Sydney to grow at [redacted] between FY2019 and FY2030 in the baseline scenario, and at an average annual rate of [redacted] between FY2019 and FY2030 under the Crown proposal.

Crown argues that there is considerable scope to increase Sydney's share of the international VIP market. Melbourne's current share of Australia's international rebate market is close to double that of Sydney. They also point to the current level of annual international overnight visitors to Sydney, which are 55% higher than Melbourne (Crown Financial Submission, p. 36).

According to Crown, the interstate rebate market currently accounts for [redacted] of total gaming revenue at The Star, accounting for the smallest segment of the gaming revenue market. Crown expects interstate rebate gaming revenue to grow [redacted] per annum between FY19 and FY2030 in the baseline scenario. Under their proposal, Crown forecast that interstate rebate revenue will be [redacted] below Melbourne's interstate rebate market, implying an average annual rate of [redacted] between FY19 and FY2030 under the Crown proposal.

According to Crown, the local non-rebate VIP market currently accounts for [redacted] of total gaming revenue at The Star. Crown expects local non-rebate VIP gaming revenue to grow [redacted] per annum between FY2019 and FY2030 in the baseline scenario. Under their proposal, Crown forecast that local non-rebate VIP revenue will reach [redacted] above Melbourne's interstate rebate market, implying an average annual rate of [redacted] between FY2019 and FY2030 under the Crown proposal. Crown points to several factors to argue that local non-rebate gaming revenue has the potential to be higher in Sydney than Melbourne, including its larger population, higher average household incomes and higher propensity to participate in other forms of gambling.

## 3.1 DAE's assessment

In the following analysis of economic and taxation impacts, **DAE accepts that the proposed growth rates expected to be achieved by the Crown operations, assuming successful implementation of their business model) are reasonable**, both in the ramp up phase between 2019 and 2022 and over the longer term. It is important to note that the ability to achieve these growth rates depends on the ability of Crown to effectively market and promote their product internationally and particularly in Asia. Based on comparisons to the Crown track record in the Melbourne rebate market we accept that this growth is achievable.

However, the potential growth of Sydney's local non-rebate VIP market and considerations of how this will impact the existing casino offering will depend on the definition of VIP applied to Crown's operations. As a general point, it is our understanding that Crown is targeting more of the ultra-high net worth individuals from Asia whereas The Star caters for this market as well as the high net worth individuals and the rising Asian middle class. As such their products, while they do overlap, are differentiated to a certain extent (mainly by the broader appeal of the integrated resort offering that includes the main gaming floor and entertainment options at The Star). Further, the expected growth in the target markets suggests that the market growth potential reduces the impact of Crown on The Star.

To this point, Crown anticipates that the expected growth in the rebate and non-rebate VIP gaming market caused by the Crown Sydney development will also generate benefits for The Star. Crown does not expect that its proposed gaming facilities will restrict The Star's revenue sources. Rather, it is assumed that The Star's gaming revenue will rise, relative to what it could expect if the Crown Sydney development does not proceed. The expectation that the presence of Crown Sydney will help stimulate the rebate and local non-rebate VIP table gaming markets in Sydney is the justification for this assumption. The joint success of Singapore's two new casinos, as outlined earlier, are illustrative of this point.

**However, Crown's assumed growth rates for The Star in the baseline scenario are not accepted in this analysis.** Crown's assumed growth rates for The Star in the baseline scenario are reported in nominal terms. Adjusting for inflation, the growth rates reported for interstate rebate players, local non-rebate VIPs and main gaming floor revenue are only marginally positive overall.

DAE considers that this very low assumed growth rates for The Star is unlikely for the following reasons:

- Sydney's population, as well as the overall visitations from the Asia-Pacific region, is forecast to grow; and
- The Star has demonstrated noticeably higher rates of growth over the past few years as a result of recent investments in the facility (completed in 2012/13), and the benefits of this investment are likely to continue for some years.

As such, DAE suggests that a reasonable overall nominal market growth rate in the baseline would be 5.5% over the longer term. This is based on a fairly mechanical calculation. Total gaming revenues are assumed to increase in line with Treasury's projections for tax revenues to the end of the forward estimates period in FY17, at 6.4% per annum. Thereafter, gaming revenues are assumed to increase with nominal GDP at a rate of 5.5% per annum. In line with Crown's modelling, the highest growth segment is assumed to be their core target market of international rebate players.

The growth rates assumed are compared by segment in Table 3.2 below.

**Table 3.2: DAE and Crown baseline revenue growth by market segment (average % p.a from FY13 to FY30)**

| | [redacted] | DAE |
|---|---|---|
| Total | [redacted] | 5.7% |
| International rebate players | [redacted] | 10.3% |
| Interstate rebate players | [redacted] | 4.0% |
| Local non-rebate VIP players | [redacted] | 4.0% |
| Main gaming floor | [redacted] | 3.0% |

Source: Crown Sydney financial model (June 2013); Deloitte Access Economics

The difference in the baseline revenue assumptions is demonstrated below in Chart 3.2.

**Chart 3.2: Baseline and proposal gaming revenue – Crown Unsolicited Proposal and DAE**

Source: Crown Sydney financial model (June 2013); Deloitte Access Economics

# 4 Economic impact

This chapter assesses Crown's estimate of the economic impact of the proposed Crown Sydney Hotel Resort and VIP only casino.

## 4.1 Crown's proposal

Crown anticipates that the proposed development will have substantial economic benefits for NSW. This section examines the following three main measures of economic impact:

- capital expenditure;
- direct employment; and
- net impact on Gross State Product (GSP).

### Capital expenditure

Crown's financial submission provides an estimated range for the likely capital expenditure associated with the Crown Sydney project. The use of a range was justified on the basis that the design of the building is yet to be finalised and the project requires planning approval.

This range is presented in Table 4.1. The estimates from the low end of this range were used as inputs for Crown's financial model and the Allen Consulting Group "Economic Benefit Assessment" that accompanies the Crown proposal.

Given these proposed values, it is estimated that a minimum capital expenditure of $1,360 million will be incurred.

In addition, Crown expects to incur ongoing capital expenditure, in the form of:

- annual maintenance costs:
  - [redacted] p.a. (FY12 terms);
  - forecast to grow by [redacted]% p.a.
- refurbishment costs every ten years, starting in FY30:
  - [redacted] (FY12 terms);
  - forecast to grow by [redacted]% p.a.

### Direct employment

According to the proposal, 1,250 people will be employed by the Crown Sydney Hotel Resort.

### Net impact on GSP

Crown's proposal provides estimates of the net impact of the development on GSP by 2021/22, the first year that Crown deems its operations will reach a more stabilised level of activity (post the initial ramp up phase). These estimates are provided relative to the following two scenarios:

- the baseline:
  - no alternative development at the Barangaroo site with The Star continuing to operate as usual (as described in Section 2); and
- an alternative development scenario:
  - development of an Australian-standard 5 star hotel at Barangaroo South

These estimates of incremental GSP are presented in Table 4.2 below. The appropriate net incremental GSP number is $565.6 million as this is the net economic benefit that takes into consideration that, should the Crown proposal not go ahead, a 5 star hotel would built on the same site.

**Table 4.2: Proposed net impact on GSP for FY22 ($m, 2012 prices)**

| | Relative to zero development at Barangaroo | Relative to Crown's alternative development scenario |
|---|---|---|
| Estimated incremental GSP | 637.9 | **565.6** |

Source: Crown Project Submission, p. 53

## 4.2 DAE's assessment

DAE acknowledges that there are uncertainties surrounding the above GSP estimates. For this reason, the impact on net GSP has been analysed under four different scenarios, as shown in Table 4.3 below.

The first scenario illustrated is simply the baseline proposed by Crown under their alternative development scenario, while Scenario 2 uses DAE's alternative baseline for

gaming revenue, as described in Section 3.1, and Crown's alternative development scenario. This scenario assumes total market growth of 5.7% rather than 3.7% used in the Crown baseline.

The final two scenarios alter the DAE baseline but use Crown's alternative development scenario. Scenario 3 examines the likely outcome using a higher win rate of 1.6%, while Scenario 4 assumes a lower outcome for international rebate player revenue, equivalent to the current market size of Melbourne.

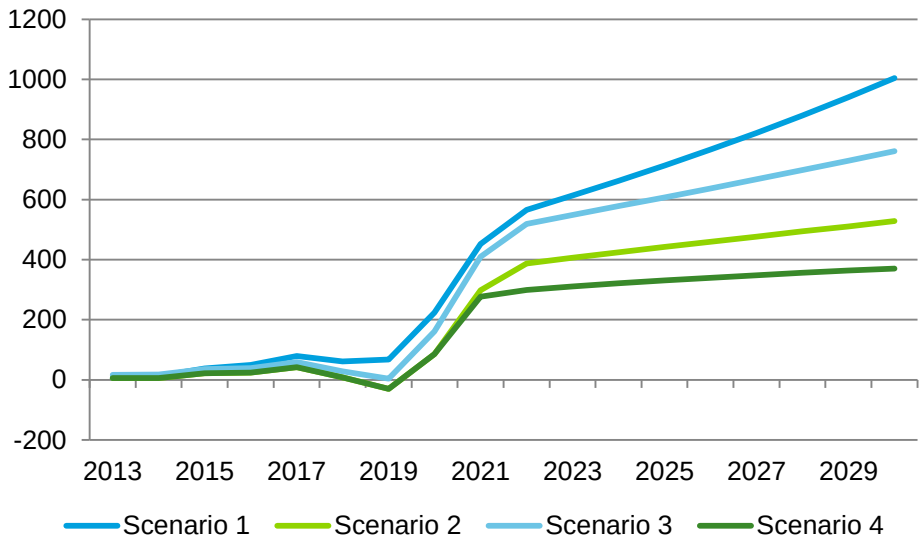
**Table 4.3: Proposed net impact on GSP relative to the baseline for FY22 ($m, 2012 prices)**

| | NPV to FY2030 | FY2022 | FY2025 |
|---|---|---|---|
| Scenario 1 – Crown proposal (net of 5 star hotel) | $3,300 | 566 | 713 |
| **Scenario 2 – DAE baseline** | **$2,212** | **387** | **442** |
| Scenario 3 – 1.6% win rate* | $3,164 | 519 | 608 |
| Scenario 4 – Melbourne international rebate player revenue* | $1,704 | 300 | 331 |

* Note: these two scenarios are modelled relative to the DAE baseline not the Crown proposal

Source: Allen Consulting Group 'An Economic Benefit Assessment'; Crown Sydney financial model (June 2013); Deloitte Access Economics

**Chart 4.1: Proposed net impact on GSP ($m, 2012 prices)**




Source: Allen Consulting Group 'An Economic Benefit Assessment'; Crown Sydney financial model (June 2013); Deloitte Access Economics

Crown's economic modelling does not include any additional tourism expenditure outside the casino and hotel complex. We have no information on the likely size of this expenditure. However, we note that there would also be some additional tourism expenditure outside the alternate 5 star hotel and, whilst they will be different types of

tourists (both in numbers and spend), we assume that the net impact of this consideration on the analysis is negligible.

As with all economic forecasts, the above analysis is subject to a number of risks.

The analysis below sets out some potential downside and upside factors which might affect the economic assessment of Crown's proposal.

Potential upside factors:

- The Crown modelling uses the 1.35% theoretical casino win rate in calculating revenue. If the win rate that is actually achieved is higher, there will be relatively larger growth in revenue (as described in Scenario 3).
- Crown modelling assumes that their offering will result in a growth in the Australian market share to [redacted]% of the international VIP market by FY2022 (up from [redacted]% in FY2012)[2]. They argue that if their product offering in Australia was very well received there is potential for capturing even greater market share.

Potential downside factors:

- Given the number of established and existing players, it might take longer for the Sydney market to develop to the size of the Melbourne market, as Melbourne has more experience in the rebate player market.
- There are a number of new casinos entering the market in other Asian jurisdictions. As such Sydney's ability to ramp up quickly (and reach forecast market share) may not be achieved.

Overall, it is expected that Crown's proposal will have a beneficial net economic impact for NSW. We would rely on the $388 million estimate of GSP in FY2022 as our central case. As demonstrated by the scenarios there is a wide range of outcomes based on the assumptions used.

[2] Source: Crown Volume 2: Financial Submission: 21 June 2013, p. 37.

# 5 Other economic and social benefits

Crown's proposal includes a number of other elements which would generate further economic and social benefits for NSW. These aspects of the proposal are briefly described in this chapter.

## 5.1 Crown's proposal

### VIP packages – access to other destinations in NSW

Crown proposes to offer high net worth customer's access to the Ellerston Day Retreat in the Upper Hunter region of NSW, and the Perisher Ski Resort. It is proposed that, among other activities, guests will have access to golf and day spa treatments at Ellerston, and private ski trips and instructor lessons at Perisher.

### Complementary tourist attractions at Barangaroo

The proposal notes that Crown is currently working with architects and designers to establish plans for other tourist attractions suitable for the Barangaroo precinct (Crown Project Submission, p. 33).

### Training colleges

Crown also proposes to establish training colleges in Penrith and Redfern, in partnership with the Penrith Panthers Group (PPG) and the National Centre of Indigenous Excellence (NCIE). Through these colleges, Crown proposes to offer apprenticeships, work experience opportunities, schools-based traineeships, cultural programs and vocational qualifications, and establish further partnerships with schools and TAFEs.

Crown proposes that these initiatives will establish employment pathways for job seekers and students in the Western Suburbs, Blue Mountains and inner-city, ultimately increasing the hospitality and tourism workforce in NSW.

### Support for Indigenous employment

According to the proposal, the creation of long-term jobs for indigenous Australians will be central to the employment strategy of the hotel resort. Crown expects that its proposed partnership with the NCIE and associated training college in Redfern, described above, will help to achieve this objective.

### Support for employment of people with disabilities

Crown proposes that the hotel resort will be committed to the provision of employment opportunities for people with disabilities, in a similar manner to Crown Melbourne and

Crown Perth. It is proposed that employees with disabilities will be assigned appropriate roles according to their circumstances and interests (Crown Project Submission, p. 150).

### Assistance to charities and community organisations

The proposal recognises the potential for the hotel resort to provide assistance to charities and community organisations, in a similar manner to the contributions made by Crown Melbourne and Crown Perth. The nature of assistance which might be provided is varied, including donations and sponsorships, provision of function rooms at a reduced price, and support through volunteer efforts of employees.

## 5.2 DAE's assessment

DAE accepts that these elements of the proposal are likely to generate additional economic and social benefits for NSW. These are not specifically included in the quantified impacts on GSP discussed in the previous chapter but need to be considered as part of the qualitative evaluation of the proposal.

# 6 Taxation impact

Crown's proposal has broad implications for state revenue. Specifically, the following revenue sources would be impacted in the event that the Crown Sydney Hotel Resort was approved:

- Gaming tax;
- Responsible Gaming Levy;
- Gaming licence fees;
- GST[3]; and
- Payroll tax.

This chapter considers the likely interaction of changes to gaming tax, the Responsible Gaming Levy (RGL) and licence fees, as a result of Crown's proposal.

## 6.1 Crown's proposal

Table 6.1 presents the two tax options that have been proposed by Crown. The tax rates listed are inclusive of gaming tax, the RGL and GST.

**Table 6.1: Tax rate options provided by Crown**

| | Option A | Option B |
|---|---|---|
| Licence fee | $100m | $250m |
| International/interstate rebate tax rate* | 10% | 9% |
| Local non-rebate VIP tax rate* | 27.5% | 23% |
| Other | Guaranteed minimum tax** | |

* Including the RGL and GST

** Guarantees that gaming taxes from The Star and Crown between 2020 and 2022 will exceed 'normalised' gaming taxes paid by The Star in 2019.

Source: Crown Project Submission, 21 June 2013

These proposed tax rates differ from those that currently apply to The Star and other gaming venues in NSW.

Each of the proposed tax rates for local non-rebate VIP revenue are below the applicable maximum tax rate of 50% under the current regime. This difference is larger under Crown's Option B. Option B also proposes a tax rate for international and interstate rebate revenue that is below the applicable tax rate of 10%.

[3] GST is collected by the Federal Government but 31% is returned to the NSW Government via the usual allocation of GST revenue grants to the States.

## 6.2 The existing tax regime

Tax rate differentials have important implications for state revenue and policy. Therefore, the tax rates proposed by Crown must be analysed within the context of the existing tax regime.

Any tax rate differentials between the regimes applied to Crown and Echo raises competitive neutrality issues. Although tax rates do not affect player odds, they create opportunities for gaming activity to shift from one location to another. A reduced tax obligation relative to The Star would provide Crown with the incentive and ability to make aspects of their offering more attractive to gaming players at The Star.

This incentive to entice players from The Star is not restricted to customers of The Star's VIP facilities. The Star's local gaming segment encompasses its main gaming floor, private gaming rooms as well as its VIP facilities. Revenue from these sources, earned from local players, is taxed collectively as part of the main regime.

As a result, there are no current tax incentives for The Star to encourage main gaming floor players to become VIPs. However, the introduction of a lower tax rate for VIP gaming at Crown Sydney would also provide an incentive for Crown to attract main gaming floor players. This could be restricted by the imposition of a strict definition for Crown's local VIP players.

Consideration does need to be given to the implications for the tax regime applicable to Echo if their exclusivity licence were to end in 2019. It is evident that Crown's proposed tax rates may potentially lead to a larger shift in gaming activity away from The Star to Crown Sydney. This will have important implications for state revenue, given the large differences between the proposed rates and the current maximum tax rate applicable to The Star's local gaming revenue over time. Furthermore, any potential change in the taxation regime for non-rebate players would have to consider any flow-on implications for gaming in club and pubs.

Possible responses to address any issues with respect to competitive neutrality of the taxation regime are not considered in this Appendix.

## 6.3 Comparison of options

The following four scenarios have been utilised to compare the implications of each option proposed by Crown for government revenue. The NPV calculations discussed in this section apply the discount rate assumed by Treasury and are based on revenue streams out to 2035.

### 6.3.1 Scenarios for analysis

**Scenario 1: Crown baseline**

Revenue forecasts are unchanged from Crown's proposed baseline scenario.

**Scenario 2: DAE baseline**

As discussed in Section 3, DAE judges that Crown has assumed an unduly low growthpath for The Star's revenue. Scenario 2 applies DAE's higher baseline illustrated in Table 3.2 and Chart 3.2.

In the UP scenario, the DAE baseline has been adopted prior to Crown entering the market in 2019 and the Crown UP estimates are applied thereafter. Note that this implies some market absorption by Crown from The Star in the baseline scenario (Chart 6.1).

**Chart 6.1: Estimate of total gaming revenue for Star and Crown under UP - Scenario 2**

**Scenario 3 – Alternative distribution between Crown and Echo under proposal**

This scenario examines the potential impact of behavioural responses due to the difference in tax rates between Crown and Echo, and the differences in the definition of local non-rebate VIP players.

As described above, all other things being equal, lower tax rates at Crown relative to Echo will tend to attract a greater share of the market to Crown. For example, under Crown's UP revenue from local non-rebate VIPs would be taxed at 27.5% (including GST) at Crown and 50% at Star (assuming the marginal non-rebate revenue from Star is taxed the highest marginal tax bracket). In FY2025, where Crown estimates that it will generate $250m in local VIP revenue, the tax differential results in a reduction in tax payable of $56m.

Under this scenario, the increase in the total Sydney market is the same as the Crown proposal, but Crown captures the entire increase in the total Sydney market above the baseline in their proposal (that is, Crown also captures uplift in revenue to Star in the UP, Chart 6.2).

**Chart 6.2: Estimate of total gaming revenue for Star and Crown under UP - Scenario 3**

## Scenario 4 – Equalising tax for The Star post 2019

This scenario considers the impact of a reduction in The Star's tax rate for rebate revenue from 10% to 9%, to align with the tax rate for Crown, if Option B was selected.

This scenario is otherwise equivalent to Scenario 2, and assumes no behavioural response.

### 6.3.2 Comparison results

Table 6.2 shows the NPV of tax collected under Option A and Option B for each of the four scenarios outlined above.

**Table 6.2: NPV of total direct tax and licence fee (to 2035, $m)**

| | Option A | Option B | Difference |
|---|---|---|---|
| Scenario 1 – Crown baseline | 655 | 702 | -48 |
| Scenario 2 – DAE baseline | 442 | 487 | -48 |
| Scenario 3 – Higher Crown local market share* | 386 | 418 | -33 |
| Scenario 4 – Lower future tax rate for Star* | 439 | 457 | -18 |

* Modelled using DAE baseline

Source: Crown Sydney financial model (June 2013); Deloitte Access Economics

Assuming that the differential tax rates would not lead to a shift in gaming activity from The Star to Crown Sydney (Scenario 1), selection of Option B would attain a higher NPV for the NSW Government. The size of this benefit narrows using a higher baseline (Scenario 2), although the difference between the two options in this case remains the same.

However, if Crown can be expected to capture a larger market share of the local non-rebate VIP market than assumed in their proposal, the incremental benefits of Option B falls compared to Scenarios 1 and 2. The NPV of this option is reduced further.

Taking into account potential changes to the international rebate tax rate for The Star from 2019 onwards, the NPV of the proposal also falls compared to the DAE base line, and the gains from Option B over Option A fall to approximately $18 million.

## 6.4 DAE's assessment

The optimal choice will depend on the relative importance of various considerations. Based on our assessment, the relative advantages of **Option B** are:

- Option B provides a higher NPV of taxation under the four scenarios presented in Section 6.3.
- Option B also provides a larger upfront licence fee, which may be preferable if the government is risk adverse.

However, for **Option A** the relative advantages are:

- Option A allows the NSW Government to capture a greater share of any upside if Crown succeeds.
- There are greater concerns around competitive neutrality under Option B compared to Option A. In particular, there are stronger incentives for Crown to attract local players from Star's VIP and main gaming floors under Option B because the differential between the marginal tax rates on non-rebate players at Star and Crown is larger.
- It is difficult to design a regime for Star that addresses competitive neutrality issues and is revenue neutral post 2019 under Option B, and there would also be potential implications for the taxation of clubs and pubs.

Given the level of risk, the modest differences in NPV, and the implications for other tax regimes post 2019 for Star, it appears that **Option A** may generate the greatest benefits for the NSW Government. The higher tax rates presented in this option will allow the NSW government to capture a greater share of any upside, particularly given the implications for gaming tax regimes beyond 2019.

# Limitation of our work

## General use restriction

This report is prepared solely for the internal use of the Steering Committee formed by the NSW Department of Premier and Cabinet to assess the unsolicited proposal by Crown. This report is not intended to and should not be used or relied upon by anyone else and we accept no duty of care to any other person or entity. The report has been prepared for the purpose of providing advice to the Steering Committee formed by the NSW Department of Premier and Cabinet to assess the unsolicited proposal by Crown. You should not refer to or use our name or the advice for any other purpose.

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# KEY ATTRIBUTES OF THE CROWN SYDNEY PROPOSAL

## Crown Sydney Hotel Resort

- Iconic hotel resort designed by the world-class architect, Wilkinson Eyre
- Located on the northwest corner of Barangaroo South
- Six-star luxury hotel
- Approximately 350 hotel rooms and suites
- 80 luxury apartments
- Five restaurants and three bars
- Luxury retail outlets
- Luxury pool and spa facilities
- Conference rooms
- VIP guest access to regional tourism venues at Ellerston Retreat and Perisher Ski Resort
- Total project cost of up to approximately $1.4 billion
- Hotel, food and beverage expected to open in 2018

## Project Partners

- Project partners include National Centre of Indigenous Excellence, Penrith Panthers Rugby League Club, United Voice (NSW Branch) and Mission Australia

## Significant economic benefits

- Gross State Product (GSP) is estimated to increase by $638 million in FY22
- Crown Sydney will directly employ c.1,250 full time employees
- Employment is estimated to increase by between 2,300 to 3,300 in FY22 (including indirect employment)
- Export income is estimated to be $513 million higher than in Crown Sydney's absence in FY22
- Business investment is estimated to increase by $151 million in FY22
- Business investment during construction is estimated to increase by $381 million in FY17
- Additional payroll tax revenue of approximately $100m over the first 10 years of full operation (FY22 to FY31)

## Training facilities

- Establishment of training colleges at Penrith—at the Penrith Panthers Group's proposed community centre
- Redfern—at the National Centre of Indigenous Excellence training facility

## VIP gaming

- Non-exclusive VIP Gaming Licence to be issued following the introduction of the necessary legislation and receipt of relevant approvals
- VIP Gaming Licence expected to commence on 14 November 2019, following the expiry of Echo's exclusivity arrangements
- Expiry date for the VIP Gaming Licence will be the expiry date of the lease for the site (the lease will be for a 99 year term)
- VIP Gaming Licence terms include:
  - No poker machines
  - No low limit tables
  - Members only – no general public access
- VIP gaming may include the operation of traditional table games, semi-automated table games and fully automated table games
- The total floor space occupied by table games must be the lesser of:
  - 20,000 sqm; and
  - 20% of the total gross floor area of the building

  No limit on the number of table games subject to the above floor space limit
- An estimated 120 tables upon opening, subject to design and planning approvals