

3-20-12

Rank-and-file Rhode Island lawmakers were unaware that 38 Studios was in the running for \$75 million when they took up the Job Creation Guarantee Program on the House floor on April 16.



Costantino says he knew of 38 Studios' interest, but neither he nor Fox, nor Stokes, when he testified for the bill, mentioned it.

Costantino

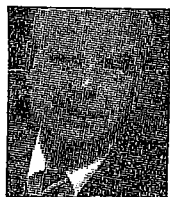
Knowing a company is interested is a lot different than knowing a company was going to get [funding]," Costantino explained later in 2010.

But Robert Watson, the House minority leader, and others objected.

"Scandal finds money," Watson warned his colleagues during the floor debate. "Scandal finds a pool of \$125 million with sketchy strings attached. Scandal will find this bill someday."

Costantino reassured colleagues that this was merely "to guarantee debt ... this is not a loan."

"The debt-service payments," he said, "will be paid by revenues from financed projects." But Republican



Ehrhardt

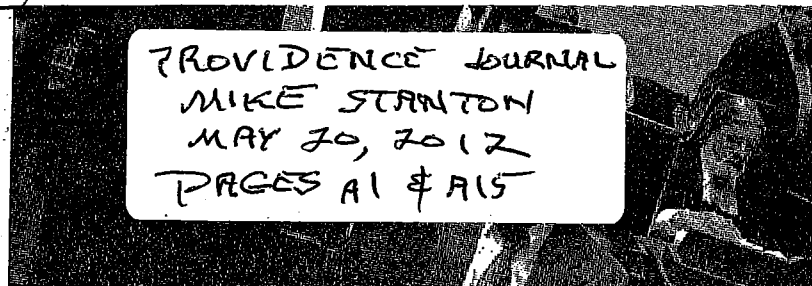
Rep. Laurence Ehrhardt of North Kingstown, while supportive of the concept, voiced concern that there was insufficient scrutiny and "no limitation whatsoever" on how much of the \$125 million could go to any one company. He fretted that a taxpayer guarantee "could turn into a need for the state to come up with the cash should the guarantees be made for unsuccessful ventures."

Costantino countered that defaults were rare. The EDC, he said, "has been very, very successful in reducing the risk to the state.... They go through a very intense risk assessment."

House Majority Leader Nicholas Mattiello chimed in, telling lawmakers: "This is a great economic development tool.... This is job creation, economic development. It's the beginning."

The loan-guarantee program won House approval that day, by a vote of 66 to 6. The legislation would also sail through the Senate, where Finance chairman Daniel DaPonte said he, too, was unaware that Schilling was close to a \$75-million deal with the state, and expressed surprise when he heard the amount.

"Now," Ehrhardt had warned his colleagues, "we are opening Pandora's box."



THE PROVIDENCE JOURNAL / CONNIE GROSCH

House Majority Leader Nicholas Mattiello, left, and House Minority Leader Robert Watson, right, (shown in April 2011) differed on the loan program.

it would bring 450 high-paying jobs and millions of dollars in income-tax revenue to Rhode Island while serving as a magnet to attract other high-tech firms to Rhode Island.

Responding to criticism from Democratic Rep. Charlene Lima of Cranston, Stokes wrote her that the EDC has gone to "great lengths to safeguard Rhode Island taxpayers." 38 Studios would receive only about \$51 million of the bond proceeds; another \$20 million or so would be held in reserve by the state to cover the first three years of debt payments.

If the company failed to reach its goals, Stokes said, it would be cut off and also penalized \$7,500 annually for each of the 450 "high-wage, high-skilled jobs it falls short of creating."

Stokes said the deal had been carefully vetted by the EDC board, which included Rhode Island's "top business, labor, higher education and civic leaders," and that a "lengthy and comprehensive due diligence" had concluded that 38 Studios was "a sound company in a high-growth interactive entertainment market projected to reach \$124 billion by 2013." In addition to annual fees from 38 Studios and income-tax revenue from its workers, Stokes said the state stood to reap \$15.25 million to \$18.8 million from the company "based on a percentage of its profits."

In the "unlikely event" of failure, Stokes reassured Lima, the EDC had first rights to all of 38 Studio's assets, including intellectual property and rights to any games it was producing.

"This ensures that under no circumstances would taxpayers be asked to repay \$75 million."

The bonds were sold to private investors, in minimum increments of \$100,000, in the fall of 2010.

Over the next 12 months, as 38 Studios moved into downtown Providence and hired 250 employees; the state disbursed \$49 million to the company.

Early this year, 38 Studios re-

leased a role-playing fantasy game that had been developed at its Maryland studio, "Kingdoms of Amalur: Reckoning," to widespread publicity and generally favorable reviews, many of which noted Schilling's role. Given the intricacies and secrecy of distribution agreements and rights fees, it's hard to know how much profit 38 Studios reaped from the rollout as it geared up for its much more ambitious Copernicus game.

Chafee says 38 Studios executives spoke optimistically at last week's EDC board meeting of how Kingdoms of Amalur has sold, "but I think differently."

"The bottom line, after all the dust has settled, is that Kingdoms didn't perform," said Chafee, adding that he has made his own inquiries in recent weeks.

Ironically, given the controversy over the size of the state's deal with 38 Studios, executives said they were also hamstrung by the fact that they received only \$49 million to build the company, not the full \$75 million to put toward the massive costs of game development. In recent weeks, 38 Studios representatives have pressed that case to state officials, according to the EDC's lawyer, David M. Gilden.

Chafee, who was relying on the EDC to monitor 38 Studios, thought that "things were going well" until his alarming meeting in April with Schilling at 38 Studios. Then, when 38 Studios missed its May 1 payment and the matter went public the following week, the spotlight was focused not only on the deal, but on the EDC's oversight.

The EDC and 38 Studios signed a "project monitoring agreement" that calls for an independent third party to monitor and report on "the development schedule and budget for Copernicus" to assure that it remains "on time and on budget," according to the private placement memorandum to potential bond buyers on Oct. 22, 2010.

IBM was chosen as the third-party

doubt about the co continue as a goir

Gilden says he that audit, or wt have done to encc 38 Studios' attemtional private func

In late Novem says 38 Studios t Stokes about a pla financing, which have to be inforr Dec. 3, he says, 38 back that they we time being and dic us anymore."

Citing confiden clined to say if 38 fact, obtained the j

With Stokes' week, Chafee has the beleaguered EI choosing a succes for the governor's t EDC know and do dios?

The EDC's outs verman, has been j to audit the books determine how the spent and whethe state bond money t own personal inv would be a violat land's agreement. S remained mum, wa book page last TI didn't.

Chafee, who as g to grapple with fina Central Falls, E; Woonsocket and now finds himself fate of the mythical;

On Friday aftern Chafee revealed the nicus' projected rel 2013, 38 Studios po line previewing th tings of the game, w the work of two of t ecutives, or "vision comic book artist J and bestselling fant Salvatore. The gamtasy world where th der siege and th choose between sav. ing it.

Asked at a news day if he could see th deal like this again, "Never. Never. Not

With reports from porter Katherine Gr