John Hogbin

6th February 2011

Submission on the Draft Report Investigation into the ACT Racing Industry
by the Independent Competition and Regulatory Commission
GPO Box 296
CANBERRA ACT 2601

Dear Commissioner,

I am writing to you because I am concerned that the Commission's draft Report into the ACT Racing Industry may not have met fully the Terms of Reference (TORs).

I write to you not in the role of a representative of any racing body or corporation, but rather as a racegoer, punter, and occasional horse owner. I am a member of both the Canberra Racing Club and the Queanbeyan Racing Club. My comments relate primarily to thoroughbred racing.

Which TORs Are Not Fully Addressed?

The Commission's TORs require that an investigation is made into, and recommendations made on, the appropriate system of product payments, and the appropriate funding outcome for the ACT racing industry. I do not believe that the TORs are adequately addressed by the analysis leading up to draft findings 3.1 (*It is appropriate that product fees continue to be calculated on the basis of gross revenues associated with ACT race events*), and 3.2 (*The rate at which the product fee is set (10%) appears to be appropriate. However, over time it may be appropriate to increase the rate in line with other jurisdictions*).

I suggest there are four tasks to be done by the Commission before conclusions can be drawn on these particular TORs.

First, an analysis should be made of of the gross revenue that Canberra racing generates Australia wide, so that an adequate long term product fee can be calculated. Second, there needs to be an assessment of what it <u>costs</u> to run racing in Canberra. Task Three is to confirm that Canberra racing is run efficiently. Task Four is then a simple calculation of what a national product fee for Canberra racing should be. I will look at these four tasks in more detail.

While clearly the Commission is an ACT body, the product fee issue is a national one, as acknowledged in the draft Report. The Commission should look at a what a mature, national, product fee regime will probably look like, and then make recommendations on what should be done by the ACT Government in the interim.

Gross Revenue Generated by ACT Racing

If the Commission believes that the product fees that have been received to date (Table 2.3) are sufficiently mature and complete to estimate continuing annual returns, then the task of calculating national gross revenue from ACT racing is simple. If the Commission however believes these figures do not yet reflect the contributions from all operators, reasonable estimates of the various components should be able to be made on available data. For example, turnover by the three TABs on ACT races is available from the results section of their websites. Estimates of corporate bookmaker turnover on ACT races could be made using published turnover figures, against which could be applied known TAB percentages for the proportion of betting on ACT racing compared with all other racing venues.

The draft Report looks at product fee rates in the ACT and elsewhere, but does not examine the 'notional' product fees that are hidden in the types payments shown in Table 3.1 under 'TAB and racing industry funding arrangements'. The Commission may wish to estimate what

these 'arrangements' amount to in total, as a way of validating the calculations made on the basis of suggestions in the previous paragraph.

Costs of Running ACT Race Meetings

Details of major cost areas areas are available from annual reports of the Canberra Racing Club. Cost areas include prizemoney, maintaining buildings and infrastructure, maintaining racing and training tracks and associated facilities, payments to jockeys and race day staff, and insurances. To some extent these costs are offset by nomination fees, annual membership fees, entry fees (on major days), food and liquor sales, and rent for non-racing use of race club facilities.

Some racing functions are best handled centrally, including handicapping and probity/safety. Centralised costs would also need to be estimated - State and National racing administrations should be willing to provide this data.

Bench Marking

It cannot be assumed that that all racing clubs and jurisdictions are run efficiently. For some jurisdictions, there had been little incentive to trim costs, chase non-wagering revenue, or make hard decisions between alternative spending priorities. This comment does not now apply to many country and regional clubs, which for some years have received their wagering-based funding based on betting turnover on the meetings which they run. As the draft Report indicates, this has not been the case with ACT racing, as the percentage of ACTTAB turnover was expressed (until mid 2010) as a percentage of all, Australia wide, wagering on racing.

None of the above suggests that ACT racing is not run efficiently. My impression of the Canberra operation over the last few years is that major in-roads have been made into costs. On the revenue side, initiatives have included the sell off of Club land to a tourism operator, and the leasing of spare Club facilities to private companies.

Nevertheless, the Commission would want to assure itself that the cost base of Canberra racing is lean and efficient, before it used that cost base to derive a minimum product fee needed for ACT racing. Benchmarking against roughly equivalent race clubs is probably the best approach here. Candidate clubs may include Kembla Grange and Newcastle in NSW, and Bendigo and Ballarat in Victoria.

Aspects of the Canberra Racing Club's operation to be benchmarked might include:
-administration costs as a proportion of turnover,
-ratio of funding that is paid out in prizemoney,
-head counts of administration staff compared with number of race meetings run,
-track maintenance costs to turnover, to number of meetings held, and to number of horses trained on the track,
-travel costs as a percentage turnover.

Summary of the Proposed Process

The process I am suggesting can be summarised as:

1. Estimate the annual gross revenue that is generated Australia wide by Canberra races.

2. Assess costs to the Canberra Racing Club of operating for one year

3. Benchmark the Canberra operation.

4. Estimate the Australia-wide product fee required to support an efficiently run Canberra racing operation.

The Process From a TAB's Viewpoint

The business model of a TAB in a fully-product fee environment might rely on a break up gross revenue (averaging 16% of turnover now) in the following manner:

-administration, computer, call centre costs and profit/tax-8.5 cents
-payment to retail outlets – 2 cents
-product fee to race clubs for racing product- 4 cents (equates to 25% of gross revenue for TABs which pay back 16%)
-0.5 cents to state and national racing bodies for central racing tasks
-Payment to local State for 'licence' to operate – 1 cent

In this example, a TAB would want assure itself that the total of 4.5 cents for the racing industry is enough – all TABs want a continuing supply of good quality product to sell. The suggested analysis by the Commission will determine that question of what it costs to run racing.

An average Friday meeting at Canberra can be used as an example to see how the 4 cents from TABs (a smaller takeout from turnover for exchanges and bookmakers) might work. If the Australia-wide turnover on an average Canberra Friday meeting was $3.6m (all operators), then $144,000 could be about the product fee amount at 25% of gross revenue (4% on turnover from TABs, a smaller % of turnover from exchanges and bookmakers).

This $144,000 would pay for prizemoney of $112,000 (eight races at $14,000), jockey fees (less nomination fees), plus the other race day costs as well as costs that are more fixed in nature.

Clearly the Canberra Racing Club would need more than the balance after prizemoney from that 'average' meeting of $32,000 to survive. It would have to look to its other revenue sources over a year to make up the difference – including hospitality sales and sponsorship. This is similar to the equation that country and regional thoroughbred clubs are faced with when they are allocated funds from their respective State racing bodies today.

In short, an open, all product fee regime should suit wagering operators, as it will guarantee supply of the product on which their customers bet. All racing clubs will have to be efficient, and look for additional revenue sources, to survive.

Phasing In of a Product Fee Regime for ACT Racing

What is the best strategy to fund Canberra racing until a national product fee regime is agreed? The Commission could recommend an indefinite continuation of the four year guarantee of funding at current levels, until a national agreement can be achieved. Or alternatively, the Commission could encourage Canberra race clubs to prepare for a total product fee based future by a phasing in model, that is, having calculated in $ terms what a lean Canberra racing operation would need to survive, convert that to a notional product fee based on estimated national turnover on Canberra races, and fund racing on that basis.

Under a phasing in arrangement, the Canberra Racing Club should have an incentive to increase its income through increased national turnover – more notional product fees, more income. While the guaranteed funding might look like a temporary subsidy from an ACT-only viewpoint, it would not be a subsidy from a national perspective. The onus would then be on the ACT Government to press all States/Territories toward early resolution of the product fee issue. Perhaps the Commonwealth Government could be approached to provide a forum to reach national consensus on this matter.

In the interim, until a national product fee regime is introduced, the ACT Government will be comforted by the knowledge that its TAB provider, ACTTAB, will not be paying its fair share of racing costs in other jurisdictions – Table 3.1 shows this to be the case, although the exact amounts are not immediately apparent from that table.

A rough estimate of the amount of product fee that ACTTAB should be paying for its racing product but isn't can be calculated as follows:
(annual ACTTAB Turnover x .75 x .98) x (.045 -.015)
where:
-.75 is thoroughbred racing's percentage of ACTTAB turnover based on initial product fees,
-.98 estimates the proportion of ACTTAB turnover that is generated by jurisdictions outside the ACT,
-.045 estimates the true cost of running racing anywhere in Australia, and
-.015 estimates the product fees due to other jurisdictions under current legislation.
(i.e., the percentage on turnover that ACTTAB under-pays for using the product of other jurisdictions is 4.5% less 1.5% or 3% on these estimates)
On an ACTTAB annual turnover of $215m, based on the above assumptions/approximations, this ACTTAB under-pay for thoroughbred racing only comes to $4.74m.

The draft Report warns against excessive product fees which may drive operators off shore. My argument is that there is a cost to run races which has to be paid. Minimising product fee leakage will provide all jurisdictions with a number of challenges, of which one is off shore operators. State-based TABs have used strategies in the past to combat overseas agencies, with some success. The US has apparently been successful in the past couple of years in preventing US bettors from accessing overseas, specifically UK, bookmakers.

It needs to be kept in mind that, on the question of increasing the product fee to some amount above 20% (pp 41-41 of the draft Report), the TAB takeout to the racing industry in most states is now much more than 20% - it is hidden in old arrangements – summarised in the second column in Table 3.1 of the Report.

Conclusions

There is a cost in providing a high standard racing product on which punters will bet. Racing cannot be run on the cheap – the true (net) cost should be identified, and this cost then expressed as a percentage of national racing 'gross revenue'. Most of this cost must be borne by the wagering bodies – TABs, exchanges, corporate bookmakers.

This approach gets away from any idea of subsidies, and avoids arguments about how many full time workers are employed in the racing industry. Further, a fully product fee based environment would give visibility of funding. The racing clubs can then get on and run races that attract betting turnover, and be paid for it. Canberra racing is taken out of the game as far as race meetings that it cannot control.

None of the above excludes the ACT Government from subsidising racing if it wants to for cultural, prestige, or similar reasons. For example, if the Canberra Club was to have difficulty in funding for replacement grandstands or racing surfaces, the government may make a once off payment. Indeed, it may be politically savvy to be seen to bolster a sporting industry that has shown it can largely pay its way.

Sincerely,

John Hogbin