

CALIFORNIA HORSE RACING BOARD

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PARI-MUTUEL AND WAGERING COMMITTEE MEETING

of the **California Horse Racing Board** will be held on **Wednesday, December 14, 2016**, commencing at **10:00 a.m.**, in the Finish Line Room at the **Los Alamitos Race Course, 4961 Katella Avenue, Los Alamitos, California**. Non-committee Board members attending the committee meeting may not participate in the public discussion, official committee vote, or committee closed session.

AGENDA

Action Items

1. Discussion and action regarding **procedures for the auditing of advance deposit wagering (ADW) in California, pursuant to Business and Professions Code section 19604 (d)(2) (D); and the requirement for additional audits, submission of financial statements or other information, inspections or investigations as may be required by the Board as authorized under CHRB Rule 2071(f), License to Conduct Advance Deposit Wagering by a California Applicant.**
2. Discussion and action regarding the **presentation from the California licensed advance deposit wagering (ADW) providers (NewCo Ventures North America, LLC, dba NYRabets.com.; Lien Games Racing, LLC.; Churchill Downs Technology Initiatives Company, dba Twinpires.com; Watch and Wager.Com, LLC.; XpressBet, LLC, and ODS Technologies, L.P., dba TVG.) regarding proposals for ADW companies to contribute to the racing industry in California.**
3. Discussion regarding the **requirement for California Advance Deposit Wagering (ADW) applicants, as a condition of licensure, to have a direct contract with CHRIMS, to provide reconciliation of ADW revenue.**
4. **General Business:** Communications, reports, requests for future actions of the Committee.

Additional information regarding this meeting may be obtained from Mike Marten at the CHRB Office at Los Alamitos Race Course, 4961 Katella Avenue, Los Alamitos, CA, 90720; telephone (714) 820-2748; cell (714) 240-1870; fax (714) 821-6232. A copy of this notice can be located on the CHRB website at www.chrb.ca.gov. *Information for requesting disability related accommodation for persons with a disability who requires aids or services in order to participate in this public meeting, should contact Mike Marten.

PARI-MUTUEL AND WAGERING COMMITTEE

Commissioner George Krikorian, Chairman
Chairman Chuck Winner, Member
Rick Baedeker, Executive Director
Jacqueline Wagner, Assistant Executive Director

DISCUSSION AND ACTION REGARDING PROCEDURES FOR THE AUDITING OF ADVANCE DEPOSIT WAGERING (ADW) IN CALIFORNIA, PURSUANT TO BUSINESS AND PROFESSIONS CODE SECTION 19604 (d)(2)(D); AND THE REQUIREMENTS FOR ADDITIONAL AUDITS, SUBMISSION OF FINANCIAL STATEMENTS OR OTHER INFORMATION, OR INSPECTIONS OR INVESTIGATIONS AS MAY BE REQUIRED BY THE BOARD AS AUTHORIZED UNDER CHRB RULE 2071 (F), LICENSE TO CONDUCT ADVANCE DEPOSIT WAGERING BY A CALIFORNIA APPLICANT.

Pari-Mutuel and Wagering Committee Meeting
December 14, 2016

ISSUE

Under Business and Professions Code section 19604 (d)(2)(D) CHRIMS performs a reconciliation of the Advanced Deposit Wagering (ADW) handle and charges a fee to the ADW companies for this service however some ADW companies pay a fee for the services, but, not all ADW companies pay the fee or they pay a fee that they feel CHRIMS should receive for this service. This highlights the necessity for CHRIMS and the ADW companies to negotiate a formal agreement for the performance of these services. If an agreement cannot be reached with all ADW companies, those that do not agree should engage an auditor with the necessary expertise to attest to the validity of the numbers submitted by the ADW companies. Regardless of who is conducting these audits, the auditing firm shall provide an independent "agree-upon procedures" audit for each California racing meeting within 60 days of the conclusion of the race meeting to the attention of the CHRB Audit Unit.

Furthermore, ADW companies are required to submit their audited financial statements when they apply for licensure. Generally, ADW companies do comply with the financial statement requirement; however, due to a loophole in the application for license to conduct ADW wagers forms CHRB 132 for instate companies, and CHRB form 133 for out of state companies, ADW companies provide consolidated financial statements that often include financial information of its parent company which lumps the parent company and all of its subsidiaries financial data into one report. Consequently it is not clear from the financials provided whether the ADWs operations in California are viable. The Board may require ADW companies to provide a profit and loss statement of its operations in California; however, a discussion needs to take place to agree on the procedures and methodology to allocate revenue and expenses to handle generated from the ADW's operations in California.

Additional audits, inspection or investigations that the Board may direct include the following:

- Auditing of the interest bearing accounts per CHRB Rule 2082, Interest Bearing Accounts
- Status and management of inactive accounts
- Inactive accounts transferred to the California State Controller's Office as unclaimed property

Overview of ADW handle, distributions, and ADW provider's fees.

The ADW companies generate handle from wagers placed by California residents on races conducted in California and races conducted outside of state. ADW handle is also generated from wagers placed by out of state patrons on races conducted in California. CHRIMS reports show that year to date California residents wagered \$582,274,301 on races conducted in and out of state and out of state patrons wagered \$277,094,515 on races conducted in California. The total ADW handle is \$859,368,821.

From of the total handle generated by ADW companies \$683,295,676 was payable to the public and \$176,073,145 was retained as takeout. *Table 1. Distribution of Takeout for Wagering Facilitated by Licensed CA ADW Providers* shows the distribution of wagers generated by California residents on races conducted in and out of the state and wagers placed by patrons out of state on races conducted in California.

Table 1. Distribution of Takeout for Wagering Facilitated by Licensed CA ADW Providers

Distribution	California Bets		Bets Placed Outside CA		All ADW bets placed in CA plus ADW bets placed outside CA on CA races	
	\$	% of Handle	\$	% of Handle	\$	% of Handle
CHRB Support	-	-	959,254	0.35%	959,254	0
Equine Research Lab	629,700	0.11%			629,700	0.07%
DIR	171,738	0.03%			171,738	0.02%
Backstretch Fund	944,549	0.16%			944,549	0.11%
Location Fees	10,050,332	1.73%			10,050,332	1.17%
AB 480 Reserve	1,398,725	0.24%			1,398,725	0.16%
Workers Comp Fund	770,843	0.13%	909,090	0.33%	1,679,933	0.20%
Retirement Fund	1,717,710	0.30%			1,717,710	0.20%
Breeders	2,423,160	0.42%	565,518	0.20%	2,988,677	0.35%
Purses	23,692,429	4.07%	13,237,142	4.78%	36,929,570	4.30%
Track Commissions	20,365,210	3.50%	10,486,636	3.78%	30,851,846	3.59%
Expense Funds*	13,111,618	2.25%			13,111,618	1.53%
Stabling & Vanning Fund*	1,900,079	0.33%			1,900,079	0.22%
Total to CA stakeholders	77,176,093	13.25%	26,157,639	9.44%	103,333,731	12.02%
Commingled Guests	-	-	30,967,245	11.18%	30,967,245	3.60%
Hub Fees	29,369,505	5.04%			29,369,505	3.42%
Import Host Fee	12,402,665	2.13%			12,402,665	1.44%
Total to ADW providers & Out of State Entities	41,772,169	7.17%	30,967,245	11.18%	72,739,414	8.46%
Retained from Public	118,948,262	20.43%	57,124,884	20.62%	176,073,145	20.49%
Payable To Public	463,326,045	79.57%	219,969,631	79.38%	683,295,676	79.51%
Total Handle	582,274,307	100.00%	277,094,515	100.00%	859,368,821	100.00%

*Per Agreement. These special distributions reduced the amounts distributed to purses and track commissions. The portion of expense fund not needed to cover actual simulcast expenses is split 50/50 between purses and track commissions AB 480 Reserve Fund is split at year end between purses and track commission. Report generated by CHRIMS.

Next, *Table 2. ADW Company Percent of Handle* shows the market share that each ADW company has in relation to each other for comparison purposes. We can see that TVG by large is the main player in the industry followed by Twin Spires that generates handle of one half the size of TVG and Expressbet generates handle of approximately one half the size of Twin Spires.

Table 2. ADW Company Percent of Handle

ADW Company	Total Handle	Percent of Total
Game Play Network ADW	23	0%
Game Play Network ODZ	56,976	0%
Lien Games LLC	23,250,081	3%
NYRAbets	1,181,488	0%
TVG	452,890,226	53%
Twin Spires	220,447,731	26%
Watch and Wager	3,188,010	0%
Xpressbet	129,907,787	15%
Xpressbet - PMG	28,447,919	3%
Total	859,370,241.00	100%

BACKGROUND

Business and Professions Code section 19604 (d)(2)(D) states “The ADW provider shall allow the board access to its premises to invest, investigate, audit, and place expert accountants and other persons it deems necessary for the purpose of ensuring that its rules and regulations concerning credit authorization, account access, and other security provisions are strictly complied with. To ensure that the amounts retained from the pari-mutuel handle are distributed under law, rules, or agreements, any ADW provider that accepts wagering instructions concerning races conducted in California or accepts wagering instructions originating in California shall provide an independent “agree-upon procedures” audit for each California racing meeting, within 60 days of the conclusion of the race meeting. The auditing firm to be used and the content and scope of the audit, including host fee obligations, shall be set forth in the applicable agreement. The ADW provider shall provide the board, horsemen’s organizations, and the host racing association with an annual pari-mutuel audit of the financial transactions of the ADW provider with respect to wagers authorized pursuant to this section, prepared in accordance with general accepted auditing standards and the requirements of the board. Any and all reasonable costs associated with those audits shall be borne by the ADW provider.

CHRB Rule 2071 (f), License to Conduct Advance deposit Wagering by a California Applicant states "The Board may conduct investigations, inspections or request additional information from the Applicant as it deems appropriate in determining whether to approve the license.

In addition, CHRB Rule 2082, Interest Bearing Accounts states "The first \$250,000 in interest earned on California resident's Account shall be transferred annually, split between the corresponding horsemen's welfare fund and the backstretch pension plan for the benefit of the backstretch employees. Interest in excess of \$250,000 shall be transfer annually, split between the corresponding horsemen's organizations for the purses as designated in Business and Professions Code Section 19613.

RECOMMENDATION

This item is presented for Committee discussion and action.

Attached for reference is a "Glossary" of ADW Fund Descriptions and the corresponding Business and Professions Code sections.

Glossary

Fund Description for California ADW Handle

CHRB Support

(19616.51 (a) (2))

This distribution follows the same general law related to the **exporting of the signal** similar to brick and mortar locations signal export. This is the funding for the California Horse Racing Board (CHRB) in lieu of license fees. The annual formula is devised by the CHRB in consultation with industry to provide the CHRB support.

Equine Research Lab

(19604 (f) (1))

An amount equal to 0.11 percent of the amount handled on ADW wagers originating in California for each racing meeting shall be distributed to the Center for Equine Health to establish the Kenneth L. Maddy for the benefit of the School of Veterinary Medicine at UC Davis Laboratory.

DIR/Problem Gambling

(19604. (f) (2))

An amount equal to 0.03 percent of the amount handled on ADW wagers originating in California shall be distributed to the Department of Industrial Relations (DIR) to cover costs associated with its audits on California trainers' payroll. However if the amount generated exceeds the costs incurred by DIR the reduction shall be forwarded to an organization designated by the racing association to augment a compulsive gambling prevention program.

Backstretch Fund

(19604. (f) (3) (A) and (B))

An amount equal to 0.165 percent of the amount handled on ADW wagers that originate in California. One-half of the amounts shall be distributed to supplement, not supplant, the trainer-administered pension plans for backstretch personnel. The other one-half shall be distributed to supplement, not supplant, the welfare fund established for horsemen and backstretch personnel.

Location Fees

(19604 (f) (4))

With respect to wagers on each breed of racing that originate in California, an amount equal to 2 percent of the first two hundred fifty million dollars (\$250,000,000) of handle from all advance deposit wagers originating from within California annually, an amount equal to 1.5 percent of the next two hundred fifty million dollars (\$250,000,000) of handle from all advance deposit wagers originating from within California annually, an amount equal to 1 percent of the next two hundred fifty million dollars (\$250,000,000) of handle from all advance deposit wagers originating from within California annually, and an amount equal to 0.50 percent of handle from all advance deposit wagers originating from within California in excess of seven hundred fifty million dollars (\$750,000,000) annually, shall be distributed as satellite wagering commissions.

AB 480

(19604)

In the event of a reduction in satellite wagering facility commissions, the benefit would then be distributed equally as purses and commissions to all associations and racing fairs that generate advance deposit wagers, in proportion to the handle generated.

Workers' Compensation Fund (19605.75, 19605.76, 19605.77)

A distribution of 0.5 percent of the amount handled in exotic pari-mutuel pools for thoroughbred and quarter horse races conducted in California is utilized to defray the cost of workers' compensation for trainers and owners. The distribution for harness horse meets is 1.0% of the amount handled in conventional pari-mutuel pools.

Retirement Fund (19604 (i) (1) and (2)), 19604 (j)

(i) Amounts distributed under this section shall be proportionally reduced by an amount equal to 0.00295 multiplied by the amount handled on advance deposit wagers originating in California for each racing meeting, except for harness racing meetings, provided that the amount of this reduction shall not exceed two million dollars (\$2,000,000). The method used to calculate the reduction in proportionate share shall be approved by the board. The amount deducted shall be distributed as follows:

(1) Fifty percent of the money to the board to establish and to administer jointly with the organization certified as the majority representative of California-licensed jockeys pursuant to Section 19612.9, a defined contribution retirement plan for California-licensed jockeys who retired from racing on or after January 1, 2009.

(2) The remaining 50 percent of the money shall be distributed as follows:

(A) Seventy percent shall be distributed to supplement the trainer-administered pension plans for backstretch personnel established pursuant to Section 19613. Moneys distributed pursuant to this subparagraph shall supplement, and not supplant, moneys distributed to that fund pursuant to Section 19613 or any other provision of law.

(B) Thirty percent shall be distributed to the welfare fund established for the benefit of horsemen and backstretch personnel pursuant to subdivision (b) of Section 19641. Moneys distributed pursuant to this subparagraph shall supplement, and not supplant, moneys distributed to that fund pursuant to Section 19641 or any other provision of law.

(j) Amounts distributed under this section shall be proportionally reduced by an amount equal to 0.00295 multiplied by the amount handled on advance deposit wagers originating in California for each harness racing meeting, provided that the amount of this reduction shall not exceed five hundred thousand dollars (\$500,000). The method used to calculate the reduction in proportionate share shall be approved by the board. The amount deducted shall be distributed as follows:

(1) First to the welfare fund established for the benefit of horsemen and backstretch personnel, pursuant to subdivision (b) of Section 19641, and administered by the organization representing the horsemen participating in the race meeting, in the amount requested by the welfare fund. Moneys distributed pursuant to this paragraph shall supplement, and not supplant, moneys distributed to that fund pursuant to Section 19641 or any other provision of law.

(2) The amount remaining, if any, shall be utilized for the benefit of the horsemen as specified in a written agreement between the racing association that conducts the live harness race meeting and the organization representing the horsemen participating in the race meeting.

Breeders (19604 (f) (5) (A))

In general, from the amounts remaining after contractual and statutory distributions, breeders receive the same relative proportion as was generated during the prior year.

Purses (19604 (f) (5) (A))

In general, from the amounts remaining after contractual and statutory distributions, purses receive the same relative proportion as was generated during the prior year.

Tracks Commissions (19604 (f) (5) (A))

In general, from the amounts remaining after contractual and statutory distributions, tracks receive the same relative proportion as was generated during the prior year.

Expense Fund (19604 (f) (5) (E))

A contractual modification, approved by the Board, of the distribution of net market access fees which would otherwise have been distributed to track commissions and purse commissions, applicable to meets hosted by thoroughbred associations. The funds generated are distributed to NCOTWINC and SCOTWINC to cover expenses incurred in operating the off-track wagering network. Amounts not expended to operate the network equally shared between purses and tracks.

Stabling and Vanning Fund (19604 (f) (5) (E))

A contractual modification, approved by the Board, of the distribution of net market access fees which would otherwise have been distributed to track commissions and purse commissions, applicable to meets hosted by Southern California thoroughbred associations and Racing Fairs which augments the amounts distributed to the Southern California Vanning and Stabling Fund from brick and mortar wagering.

Commingle Guess

It represents the amount that is kept by out of states outlets wagering on California races, when California exports its racing signal.

Hub Fee (19604 (a) (5))

It is the portion of contractual compensation, excluding host fee payments, retained by ADW providers licensed to conduct business in California from wagers placed in California.

Import Host Fee (19604 (a) (B))

Contractual amount, generally limited to 3.5% of handle, retained by ADW Providers to pay tracks located outside of the state for accepting California wagers into their respective pools.

Retained From Public

Represents the amount kept from the public to benefit the different sectors of the horse racing industry, also known as the takeout.

Payable To Public

Represents the prizes paid as winning tickets.

Total Handle

Amount wagered in the pari-mutuel pool.

STAFF ANALYSIS

DISCUSSION AND ACTION REGARDING THE PRESENTATION FROM THE CALIFORNIA LICENSED ADVANCE DEPOSIT WAGERING (ADW) PROVIDERS (NEWCO VENTURES NORTH AMERICA, LLC, DBA NYRABETS.COM,; LIEN GAMES RACING, LLC,; CHURCHILL DOWNS TECHNOLOGY INITIATIVES COMPANY, DBA TWINSPIRES.COM; WATCH AND WAGER.COM, LLC,; XPRESSBET, LLC, AND ODS TECHNOLOGIES, L.P., DBA TVG,) REGARDING PROPOSALS FOR ADW COMPANIES TO CONTRIBUTE TO THE RACING INDUSTRY IN CALIFORNIA.

Pari-Mutuel and Wagering Committee Meeting
December 14, 2016

ISSUE

At its November 17, 2016 Regular Meeting the Board issued short-term licenses through January 2017 to each of the six Advance Deposit Wagering (ADW) companies authorized to accept wagers in California. The Board delayed issuing longer-term licenses of up to two years until those companies submit additional financial information on their current and future contributions to California horse racing, such as racing-related charities.

ANALYSIS

During discussions of ADW licenses at the November 2016 Board meeting, various commissioners asked ADW representatives questions about their profitability in California. Chairman Winner noted that the profits of the ADWs are greater than the horsemen or the associations. He pointed out that other stakeholders in California are struggling, while the perception is that ADWs are highly profitable. He stated the Board should determine the facts, and if the ADWs were doing well, the Board believed it was time the ADW providers contributed more to the industry.

Included in this discussion were statements about the number of ADW employees in California and ongoing efforts to provide for a fair distribution of revenue from wagers placed through ADW by patrons located at live race meetings.

BACKGROUND

ADW providers were asked to return with the financial information and with information regarding their contributions to California horse racing, both current and planned for the future.

RECOMMENDATION

This item is presented for Committee discussion and action.

STAFF ANALYSIS
DISCUSSION REGARDING THE REQUIREMENT FOR CALIFORNIA ADVANCE
DEPOSIT WAGERING (ADW) APPLICANTS, AS A CONDITION OF LICENSURE, TO
HAVE A DIRECT CONTRACT WITH CHRIMS, TO PROVIDE RECONCILIATION OF
ADW REVENUE

Pari-Mutuel and Wagering Committee
December 14, 2016

ISSUE

It was recently brought to the attention of California Horse Racing Board (CHRB or Board) staff that Advance Deposit Wagering (ADW) providers do not contract directly with CHRIMS for the wager reconciliation services CHRIMS provides. Furthermore, it has been conveyed that multiple ADW providers continue to not pay CHRIMS the full cost of these services at the rate CHRIMS has assessed.

BACKGROUND

Business and Professions Code section 19460 states that licenses granted under the Horse Racing Law are subject to all rules, regulations, and conditions prescribed by the board. Furthermore, the statute requires that all licenses contain "such conditions as are deemed necessary or desirable by the board for the best interests of horse racing."

CHRIMS is a not for profit, mutual benefits organization focused on providing technology solutions for the pari-mutuel gaming industry. They specialize in accounting applications and pari-mutuel settlement outsourcing, but also provide solutions for managing customer loyalty programs and admission and wager tracking. Presently, CHRIMS provides daily reconciliation services for all wagers placed through CHRB-licensed ADW providers. These services, however, are not subject to any written agreement between the ADW providers and CHRIMS. CHRIMS has assessed that the reasonable cost of the services they render to each ADW provider is \$3000/month.

ANALYSIS

Pursuant to Business and Professions Code section 19460, the Board has the authority to attach any condition it deems necessary or desirable for the best interests of horse racing on the licenses it grants. Accordingly, the Board has the option to condition the licenses it grants to ADW providers on their entering into a direct written agreement with CHRIMS to provide reconciliation services for the duration of the ADW provider's license.

RECOMMENDATION

This item is presented to the Committee for discussion.