



Ohio State Racing Commission

77 South High Street • 18th Floor
Columbus, OH 43215-6108
(614) 466-2757 FAX (614) 466-1900
www.racing.ohio.gov

Ted Strickland
Governor

William Koester
Chairman

STATE RACING COMMISSION: A PROPOSAL TO SAVE OHIO'S HORSE RACING INDUSTRY MARCH 19, 2009

The Ohio State Racing Commission ("Commission") was recently requested to provide a proposal for permitting the use of slot machines or video lottery terminals ("VLTs") at Ohio's horse racing tracks. In response to that request and the interest expressed by other parties, the purpose of this document is to provide such proposal.

Background on Ohio's Horse Racing Industry

Ohio has an extremely rich horse industry heritage. The Ohio horse population attests to the popularity of the horse industry, which generated an economic impact of \$2.185 billion a recently as 2005. Racing composes 37.5% of this economic impact.¹

In 1933, pari-mutuel wagering at horse racing tracks was authorized after passage of the "Horse Racing Act" by the Ninetieth General Assembly in an effort to raise revenues and create jobs during the depression.² Authority to conduct pari-mutuel wagering at horse racing tracks is currently contained in Chapter 3769 of the Ohio Revised Code. The Commission is the state agency that regulates such wagering.³

Pari-mutuel wagering on horse races is permitted with regard to live racing conducted at such tracks, as well as races conducted at race tracks around the world.⁴ Revenues generated from taxing such wagering not only funds the Commission, but also supports the horse race industry and related agricultural industry, as well as contributes to fund PASSPORT.⁵

¹ *Ohio Racing Industry Study*, prepared by The Innovation Group on behalf of the Ohio State Racing Commission, October, 2008, page 2. See also *The Economic Impact of the Ohio Horse Industry*, prepared by Deloitte on behalf of the American Horse Council Foundation, 2005.

² Am. Sub. S.B. 103, 90th Gen. Assem., Reg. Sess. (Ohio 1933). See also *The Michigan Horse Racing Industry, An Economic Comparison*, p. 6 (2002).

³ The Commission's primary goals are to regulate and promote pari-mutuel horse racing in the state of Ohio. To promote the racing industry, the Commission has several programs which promote breeding horses in-state and supplement purses at the commercial racetracks and county fairs for Ohio bred horses. The Commission also has significant enforcement responsibilities to protect the betting public, including the licensing of all horses and participants, on site regulation of each race and facility, the study of betting patterns, and the drug testing of horses and participants.

⁴ See current Revised Code Chapter 3769, including R.C. 3769.01, 3769.089, and 3769.26.

⁵ Ohio Rev. Code Ann. §173.40. As discussed in more detail in footnote 9 below, PASSPORT is a government program designed to help Medicaid-eligible older Ohioans get the long-term services and supports they need to stay in their homes. See "Ohio Department of Aging PASSPORT Program." *Ohio Department of Aging*, 2 Feb 2009 <<http://aging.ohio.gov/services/passport/default.aspx>>. In calendar year 2007, horse racing contributed \$2,737,000 to PASSPORT. 2008 Annual Report, Ohio State Racing Commission.

Currently, Ohio has seven horse racing tracks, three thoroughbred horse racing tracks and four standardbred (i.e., “harness”) horse racing tracks. Only New York contains more standardbred tracks.⁶ Ohio’s tracks are located throughout the state:

Track	Type	Location	Market
Beulah Park	Thoroughbred	Grove City	Central Ohio
Lebanon Race Track	Standardbred	Lebanon	Dayton/Southwest Ohio
Northfield Raceway	Standardbred	Northfield	Cleveland/ Northeast Ohio
Raceway Park	Standardbred	Toledo	Northwest Ohio
River Downs	Thoroughbred	Cincinnati	Southwest Ohio
Scioto Downs	Standardbred	Columbus	Central Ohio
Thistledown	Thoroughbred	North Randall	Cleveland/ Northeast Ohio

Some limited amounts of quarter horse racing also occurs at these Ohio race tracks.

Ohio has historically been the top standardbred horse racing state in the country and is home to one leg of the standardbred triple crown—The Little Brown Jug (held at the Delaware County Fairgrounds). In fact, the national headquarters of the United States Trotting Association is located in Columbus.

Economic Impact of Ohio’s Horse Racing Industry

The Commission estimates that at least 12,300 fulltime equivalent (“FTE”) jobs are currently generated in Ohio by the horse racing industry. Our estimate includes both direct horse racing jobs, as well as indirect jobs that support the industry (such as jobs to supply goods and services to the industry).⁷

The Commission also estimates that the current total economic impact of Ohio horse racing is approximately \$460 million.⁸

Regulation of the Horse Racing Industry

The horse racing industry is regulated by the Commission, which is comprised of five members appointed by the Governor, an Executive Director and staff. The Commission is dedicated to the

⁶ *Ohio Racing Industry Study*, prepared by The Innovation Group on behalf of the Ohio State Racing Commission, October, 2008, p. 6.

⁷ This estimate is based on the study performed by Deloitte & Touche, LLP using 2003 data, but adjusted by the Commission for industry declines since 2003 (see footnote 1). These estimates include Standardbred, Thoroughbred and Quarter horse racing related jobs. See also *Ohio Racing Industry Study*, prepared by The Innovation Group on behalf of the Ohio State Racing Commission, October, 2008, page 2.

⁸ Based on the Deloitte study, as adjusted for declines in the industry; see also *Ohio Racing Industry Study*, prepared by The Innovation Group on behalf of the Ohio State Racing Commission, October, 2008, page 2.

protection, preservation, and promotion of horse racing and its related industry components. In that connection, the Commission regulates pari-mutuel wagering and the licensing of all industry participants in order to insure the protection of the wagering public and the integrity of the sport. It uses its best efforts to promote horse racing and breeding to the citizens of Ohio, and cooperates with horse owners, trainers, breeders, other licensees, county fairs, and commercial racetracks in order to accomplish these goals. The Commission strives to create an atmosphere where the wagering public feels protected and the sport maintains the highest level of integrity.

The Commission was created in 1933 after the General Assembly approved pari-mutuel wagering on horse racing. The Commission currently employs 20 people full and part-time. Eleven work at its centrally-located Columbus headquarters, nine inspectors and investigators are assigned to commercial racetracks. The Commission contracts with eleven others, including judges, stewards, and veterinarians, who work at seven commercial racetracks. The Commission also sends its employees to and contracts with veterinarians for county fairs which have pari-mutuel racing.

Members of the Commission meet monthly to conduct business, approve racing dates, decide matters of racing importance, and mete out penalties to licensees found in violation of racing statutes and rules. Meetings are held in downtown Columbus during winter months and at most or all of the commercial tracks during the remainder of the year.

The Commission is funded entirely by taxes generated on the total amount wagered (i.e., "handle"). In addition to contributing to the Commission's budget, the tax on each track contributes money to breeding funds, a fairs fund, and PASSPORT⁹. Twenty-five percent of all taxes levied on the handle are paid into the PASSPORT fund. In calendar year 2000, PASSPORT received \$5.377 million dollars from these taxes, yet in calendar year 2008 received only \$2.737 million. As tracks close, even less money will be paid into the PASSPORT fund.

An Industry in Decline

Ohio's horse racing industry is in steep decline. Evidence of this decline is highlighted by the recent bankruptcy filing by Thistledown, located in North Randall (near Cleveland). In fact, if Thistledown is unable to meet certain minimum obligations to maintain its racing permit, the Commission will be forced to close Thistledown, resulting in 260 immediate job losses.

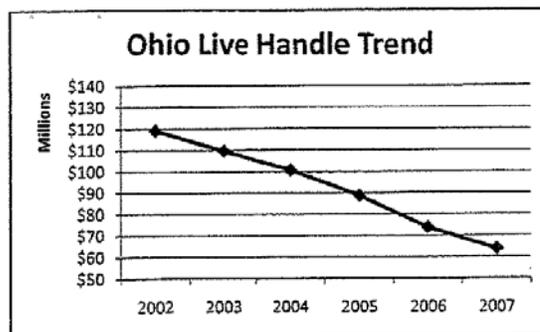
The primary reason for this decline in Ohio's horse racing industry is that surrounding states permit alternative gaming and the proceeds of such gaming is used to subsidize their racing industry.¹⁰ These subsidies have resulted in significantly higher purses in surrounding states, as well as significant incentives to breed horses in those states. As a result, we have seen a

⁹ PASSPORT is a two-pronged program administered by the Ohio Department of Aging. The first part is a pre-admission screening during which interested consumers are screened by telephone to determine preliminary Medicaid eligibility and care needs. They are also provided information about the variety of long-term care options available. The second part of PASSPORT is home care. Once a consumer is determined eligible a case manager works with him or her to develop a package of in-home services to be provided by local service providers. The case manager then monitors the care for quality and changes the care plan as necessary.

¹⁰ *Ohio Racing Industry Study*, prepared by The Innovation Group on behalf of the Ohio State Racing Commission, October, 2008, page 92.

migration of quality horses, trainers and jockeys/drivers to jurisdictions with higher purses and more owner/breeder incentives. This migration is directly tied to the competition from states with expanded gaming.¹¹

From 2002 to 2007, live handle at Ohio's thoroughbred and standardbred racetracks has decreased at an average rate of 12% to 11% per year, respectively.¹² Further, Ohio purse pools have suffered because statewide simulcast handle has declined an average of 7% per year during the same period.¹³ The following graph displays the steady nature of decline in live racing handle:



Source: OSRC; The Innovation Group.

The weak handle and lower purses have made its way into the breeding sector as Ohio breeding programs are in decline. The number of standardbred stallions in the program declined 34%, from 195 in 2002 to 128 in 2007.¹⁴

Standardbred Stallion Report Summary			
	Stallions Registered	Stallions Renewed	Total
2002	30	165	195
2003	33	140	173
2004	27	137	164
2005	27	131	158
2006	18	121	139
2007	25	103	128

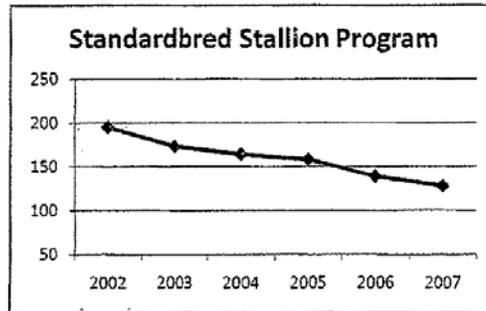
Source: OSRC; The Innovation Group

¹¹ *Id.*

¹² *Ohio Racing Industry Study*, prepared by The Innovation Group on behalf of the Ohio State Racing Commission, October, 2008, page 3.

¹³ *Id.*

¹⁴ *Id.*



Source: OSRC; The Innovation Group.

As a specific example of how this impacts the industry, two of Ohio’s premier standardbred horses—Chip Chip Hooray and Yankee Cruiser—were forced to relocate to Pennsylvania in the last couple years. As another example, Midland Acres, one of Ohio’s top breeding farms located near Washington Court House, opened a satellite stallion station in Indiana at the insistence of horse owners seeking to move their horses.

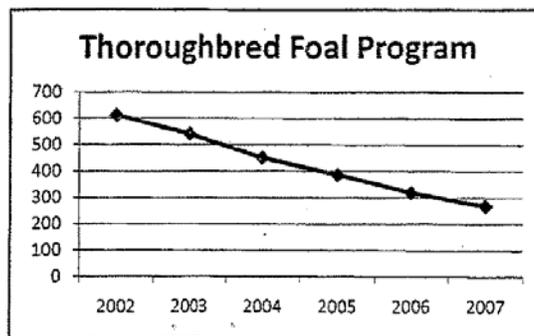
The thoroughbred foal program is experiencing an even more severe decline, as the number of foals has fallen 68%, from 612 in 2002 to 196 in 2008.¹⁵ The number of Ohio foals has been declining at a pace of 10% per year.

Thoroughbred Foal Report Summary

	Accredited	Ohio-Foaled	Total
2002	373	239	612
2003	349	193	542
2004	297	155	452
2005	224	163	387
2006	169	151	320
2007	130	139	269
2008	97	99	196

Source: OSRC; The Innovation Group

¹⁵ Ohio State Racing Commission’s Thoroughbred Registrar and *Ohio Racing Industry Study*, prepared by The Innovation Group on behalf of the Ohio State Racing Commission, October, 2008, page 4.



Source: OSRC; The Innovation Group.

The Commission believes that five of Ohio's seven horse racing tracks will close within the next several years if no action is taken by the legislature to save this industry.¹⁶

The current total economic impact of Ohio horse racing is approximately \$460 million. If Ohio loses five of its seven horse race tracks, Ohio would lose approximately \$328 million of economic impact and approximately 8,600 jobs. Based on the study performed by The Innovation Group on behalf of the Commission, alternative gaming is the only way to maintain the long-term financial stability of Ohio's horse racing industry.¹⁷

The Case for VLTs at Ohio's Horse Racing Tracks

Many proposals have been put forth to amend Ohio's Constitution in order to allow the use of VLT gaming in Ohio. Generally, these efforts have been proposed by private business interests in an effort to advance their pecuniary and commercial gain. Further, the tax rates proposed by these efforts have generally been only in the range of 30% - 35% of gross proceeds (amounts wagered less amounts paid to winners). Finally, unlike the surrounding states, recent proposals in Ohio have provided insufficient benefits to preserve Ohio's horse racing industry. While these proposals have always promised great economic benefits to the state, voters have flatly rejected these efforts to use the Constitution to further the gain of private business interests.

A February, 2008, industry analysis asserts that Ohioans contribute approximately \$1.276 billion to day-trip markets in Pennsylvania, Michigan, Canada, Indiana, West Virginia and New York.¹⁸ This estimate does not include the impact of recently opened table games at Wheeling Island (near Cambridge) and Mountaineer Park (near Steubenville) in West Virginia, nor does it include the impact from VLTs being recently added at two Indiana horse racing tracks. The study

¹⁶ See also *Ohio Racing Industry Study*, prepared by The Innovation Group on behalf of the Ohio State Racing Commission, October, 2008.

¹⁷ *Ohio Racing Industry Study*, prepared by The Innovation Group on behalf of the Ohio State Racing Commission, October, 2008, at page 98.

¹⁸ *Ohio Statewide Gaming Market Assessment: Seven Racetracks*, prepared by The Innovation Group on behalf of Ohio Legacy Fund, February 2008, at page 29.

projected that by calendar year 2010, the amount of gaming expenditures leaving the state of Ohio would increase to \$1.62 billion.¹⁹

In a recent memorandum to the Commission (attached), Commissioner Thomas Zaino discussed the history of gambling in Ohio. Based on conclusions reached in that memorandum, the General Assembly has the ability to authorize the use of VLTs at Ohio's horse racing tracks by statute, especially if such VLTs were operated by a state agency.

The experience in other states is that alternative gaming helps grow the quality of their horse racing and, therefore, the size of the horse racing industry in those states. Pennsylvania is a good example of how alternative gaming can positively impact the horse racing industry. Pennsylvania adopted alternative gaming at horse racing tracks in 2007. From 2006 to 2007, Pennsylvania realized an increase in purses earned of over 160%, from \$55.0 million in 2006 to \$144.3 million in 2007.²⁰

The Commission's Alternative Gaming Proposal

The Commission proposes that the General Assembly enact into law a statute that authorizes a state agency to conduct VLT gaming at Ohio's horse racing tracks. The purpose of having a state agency conduct the gaming is to protect state and local revenues from potential Ohio Constitutional challenges by opponents to gaming (see attached memorandum by Commissioner Thomas Zaino). Other benefits of this approach include maximizing state revenues produced by such operations and permitting the state to fully regulate such gaming.

In terms of which state agency is best suited to conduct VLT gaming at Ohio horse racing tracks, many options exist including the Ohio State Racing Commission, the Ohio Lottery Commission, or a new state agency. However, any existing agency must be reconstituted to address the unique regulatory and integrity issues associated with this type of gaming. For purposes of this proposal and because the Commission has regulated pari-mutuel wagering and horse racing tracks for decades, we will assume that the Commission will be the state agency chosen to conduct the VLT gaming.

How the Gaming Would Work: The Commission proposes that it be reconstituted and statutorily authorized to conduct VLT gaming at Ohio's seven horse racing tracks. The size of the Commission would be expanded from five to nine members. The one member would be appointed by each majority and minority party of House of Representatives and the Senate. The remaining five members would continue to be appointed by the Governor. Similar to its role today, the newly constituted Commission would meet at least monthly to provide tight oversight of the Executive Director and staff, issue rules, receive input from the public, conduct administrative hearings, and conduct all other business of the Commission.

¹⁹ *Id.*, pages 29 and 32. None of these estimates include amounts wagered in Nevada (Las Vegas/Reno) or New Jersey (Atlantic City).

²⁰ *The Economic Impact of Slot Machines on Pennsylvania's Pari-Mutuel Wagering Industry, Benchmarking the Industry: 2006 - 2007*, prepared by Kevin C. Kile, Pennsylvania Gaming Operations Liaison, at page 7.

The Commission would conduct the VLT gaming through licensed agents that also hold pari-mutuel horse racing permits, thus limiting VLTs to Ohio's seven horse racing tracks. The Commission would add approximately 150 new employees to conduct such gaming and to:

- Purchase and maintain VLT machines at facilities owned by licensed agents, in a commercially feasible quantity;²¹
- Grant a ten year license for entities to serve as commissioned agents (which must also hold a valid license to conduct pari-mutuel horse racing). The license may be renewed twice, for an additional five years for each renewal;
- Have inspectors and investigators on-site at each facility 24 hours a day, seven days a week;
- Approve all VLT games and ensure each game's integrity;
- Approve all advertising of the facilities and gaming, including the placement and amount of advertising;
- Investigate and license all direct and indirect owners and officers of the entity holding the commissioned agent's license, including fingerprinting, criminal background checks, financial background checks, and character reviews to protect the integrity of the gaming;
- Investigate and license all primary employees of the facility that have direct contact with VLT game operations or handle cash, including fingerprinting, drug testing, criminal background checks, and financial reviews, to protect the integrity of the gaming;
- Investigate and license all secondary employees of the facility, including fingerprinting and criminal background checks;
- Enact administrative rules governing gaming and all activities taking place at gaming facilities;
- Monitor betting patterns and conduct investigations of questionable betting or other activity that takes place on grounds of the gaming facility;
- Issue subpoenas requesting personal appearance or production of records necessary to enforce Commission laws and rules;
- Impose discipline upon licensees, including fines, suspensions, and/or revocation of licenses;
- Conduct administrative hearings of disciplinary actions, in accordance with Revised Code section 119;
- Coordinate with state and local officials to ensure that the gaming facilities and commissioned agents are in full compliance with all of Ohio's laws and local ordinances;
- Provide gambling addiction services and administer a Voluntary Exclusion Program, whereby certain individuals may request to be excluded from the facilities;
- Administer a minority owned business enterprise utilization program; and
- Collect and distribute revenues in accordance with statutory and administrative law guidelines.

²¹ The Commission believes that Ohio can viably support about 14,000 VLT machines. While this averages out to 2,000 machines per horse racing track, the actual amount at each track will depend on the economic and competitive conditions for each market.

The Commission would be permitted to grant licenses to be agents. Such licensed agents would earn a commission and be required to:

- Pay a license fee of \$50 million, one half to be paid upon application to be an agent and the other half due twelve months after receiving Commission approval;
- Develop, build and maintain appropriate facilities (as approved by the Commission), including a minimum up-front improvement to facilities of at least \$80 million per location;
- Pay the Commission's cost of all background checks and investigations into the character of all direct and indirect owners and employees;
- Hire and manage employees working at gaming facilities;
- Provide approved marketing of their facility at levels required by the Commission and in manners approved by the Commission;
- Provide space at the facility for the Commission to house its on-site personnel and equipment;
- Make payments into a fund administered by the Commission to be used to address gambling addiction issues;
- Comply with all applicable federal, state and local laws, ordinances, and rules; and
- Maintain a current and valid permit to conduct pari-mutuel wagering at horse racing tracks, and comply with all of the Commission's rules of racing.

How Proceeds Would be Distributed: Amounts generated from VLTs would be used to pay game winners, the operating costs of the regulatory agency, and the commissions paid to licensed agents. The remaining net proceeds generated from VLTs would be deposited into a special fund, the Gaming Profits Education Fund, that would be used only to fund elementary, secondary, special, or vocational education.

The Financial Estimates: Many previous proposals that have been on the ballot have promised dramatic positive economic and tax revenue impact for the state. To achieve those projected benefits, the previous proposals assumed what the Commission believes were very aggressive financial results. The Commission also believes the estimates did not take into account the ramp-up period necessary to actually implement the proposed gaming.

The Commission believes that once the facilities are fully operational, gross proceeds (wagers minus winnings) resulting from operation of VLTs at Ohio horse racing tracks will be approximately \$1.0 to \$1.3 billion per year. Fifty percent of the gross proceeds will be paid as commissions to the licensed agents.²² Once fully operational (in 2013), approximately two percent of gross proceeds will fund the regulatory agency. The remaining forty eight percent will constitute net proceeds and will be paid into a newly created Gaming Profits Education Fund.

In addition to the amounts described above, new revenue will also be generated from license fees and other miscellaneous fees that will be imposed on all licensees. For example, we recommend

²² This represents a lower commission than granted to lottery sales agents. For instance, lottery sales agents earn a 5.5% commission on total amount wagered at their location, plus may earn an additional 1.5% based on cashing ratios and bonuses for selling winning tickets. To compare apples to apples, the Commission's VLT plan contemplates a mere 5% commission to licensed VLT agents.

that the one-time license fee of \$50 million per horse racing track be required, which is expected to be paid over a two year period, beginning in FY 2010.²³ The following table illustrates the annual revenue estimates:

	FY2010	FY2011	FY2012	FY2013
Gross Proceeds ^{24 & 25}	\$200 million	\$440 million	\$960 million	\$1.3 billion
Annual License Fees	\$175 million	\$175 million	- 0 -	- 0 -
Total Gross Proceeds	\$375 million	\$615 million	\$960 million	\$1.3 billion
Less: Commissions ²⁶	(\$100 million)	(\$220 million)	(\$480 million)	(\$650 million)
Less: Funding of State Agency ²⁷	(\$80 million)	(\$85 million)	(\$20 million)	(\$25 million)
Net Proceeds to Fund Education	\$195 million	\$310 million	\$460 million	\$625 million

The Commission has been careful not to over-promise the financial results and economic impact of authorizing the use of VLTs at Ohio's seven horse racing tracks. The Commission strongly believes the amounts described above are viable and achievable.

²³ Current economic conditions will make it difficult for potential licensees to raise this level of capital. Therefore, we recommend that the state "finance" the license fee over a period of two years, thereby freeing up capital for the licensees to use for purposes of making necessary improvements to their facilities.

²⁴ Gross proceeds are the total amount wagered using the VLT machines, often referred to as the "handle."

²⁵ Based on our understanding of the experience in other states in getting gaming up and running, we estimate that gross proceeds will ramp up at a rate of 20% for FY2010, 40% for FY2011, 80% for FY2012 and 100% by FY2013. These percentages are applied to gross proceeds of \$1.0 billion for FY2010, \$1.1 billion for FY2011, \$1.2 billion for FY2012, and \$1.3 billion for FY2013.

²⁶ The commission paid to the licensed agents is 50% of gross proceeds derived at their facility (or approximately 5% of total amount wagered on the VLT machines located at their facility). See footnote 23 above, comparing this amount to the commissions paid to lottery sales agents.

²⁷ This figure includes the increased operating budget for the Commission and the cost of new VLT machines. We assume that the Commission will add 150 employees to tightly regulate the proposed alternative gaming and increase its operating budget by \$15 million annually. For FY2010, the entire \$15 million would be prorated as the agency adds the new employees. We also assume the cost of a VLT machines is \$10,000 each, and one-half will be paid (cash out of pocket) in FY2010 and the other half will be paid in FY2011.

Conclusion

When compared to previous and currently pending VLT/casino proposals, this proposal, which calls for giving statutory authority to the Commission to conduct VLT gaming at Ohio's seven horse racing tracks, offers significant advantages, including the following:

- When combined with reforms to the Commission's regulation of horse racing permit holders, saving Ohio's horse racing industry and preserving over 8,000 jobs that are related solely to horse racing.
- Limiting the new gaming to only those locations where gambling has been permitted in Ohio since the Great Depression—horse racing tracks. This limits its accessibility and permits tighter controls.
- Allowing for faster implementation because facilities are currently in existence, thereby accelerating the revenue and economic benefits to the state of Ohio.
- Providing the maximum effective tax rate of any current or prior alternative gaming proposal, the net proceeds of which will provide funding for elementary, secondary, vocational and special education.
- Providing for tight government controls, giving the General Assembly and Governor maximum flexibility to regulate this industry well into the future.
- Offering realistic and achievable revenue and economic projections, taking into account the current economic environment in Ohio and competitiveness of the gaming industry.
- Avoiding private business interests from using the Ohio Constitution to achieve their own pecuniary and commercial gain.
- Slowing the export of the estimated \$1.276 billion of gaming expenditures leaving Ohio for surrounding states each year.

CAVEAT: The Commission is pleased to provide this proposal to authorize VLT gaming at Ohio's horse racing tracks. However, while Ohio is facing dramatic economic and budgetary challenges, the Commission is in no way suggesting that authorization to conduct VLT gaming at Ohio's horse racing tracks is a panacea for Ohio's economic woes or school funding challenges. Rather, the Commission is merely trying to keep Ohio's horse racing industry vibrant, while providing the benefits outlined above. While such gaming will save Ohio's horse racing industry, it will certainly not save Ohio.

The Commission welcomes the opportunity to open a dialogue about this proposal and to address any related thoughts or concerns, as well as to consider improvements or other approaches to ensuring the vibrancy of Ohio's horse racing industry.