



REPORT TO GOVERNOR DAYTON AND THE MINNESOTA LEGISLATURE

NOVEMBER 2015



Minnesota Racing Commission

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EXECUTIVE SUMMARY

This Report is in response to the Legislature’s request that the Minnesota Racing Commission (MRC) “work in consultation with the racing industry to propose permanent dedicated funding changes to fully support the operations of the commission to ensure that racing is conducted in the public interest.” Laws 2015, chapter 77, article 1, section 16.

Part I of the Report briefly describes the current funding streams for the MRC.

Part II describes in qualitative terms the beneficial economic impact of the racing industry to Minnesota’s economy and recommends that Minnesota conduct a quantitative economic impact analysis of the industry as many other states have done.

Part III describes the state of the racing industry both nationally and in Minnesota. Although the leading indicators of industry health-wagering levels, size of foal crops, and number of races offered - have trended downward for several years, there are reasons for optimism. Minnesota racing has countered some of these trends and could enjoy a significant rebirth, especially with more supportive public policy.

Part IV describes three guiding principles for evaluating funding alternatives for the MRC. First, MRC should have a secure and dedicated funding source to ensure proper regulatory oversight. Second, industry participants should continue to share in funding MRC, but those cost burdens should be more equitably distributed than is currently the case. And third, given the racing industry’s contributions to the Minnesota economy and the importance of maintaining its integrity, the State should share in the responsibility for funding adequate regulatory oversight.

Part V describes ways to increase MRC funding from existing sources and proposes new revenue-producing options that would benefit both MRC and the racing industry. The MRC urges the Legislature to authorize advance deposit wagering (ADW) to generate much needed revenue for the race tracks and racing’s participants.

INTRODUCTION

The Legislature appropriated \$341,000 to the Minnesota Racing Commission (MRC) from the general fund for the 2016-2017 biennium to make up for a projected shortfall in the Commission's operating budget. The Legislature and Governor directed the MRC "to work in consultation with the racing industry to propose permanent dedicated funding changes to fully support the operations of the commission to ensure that racing is conducted in the public interest". The MRC was requested to report its findings to the Legislature and the Governor.

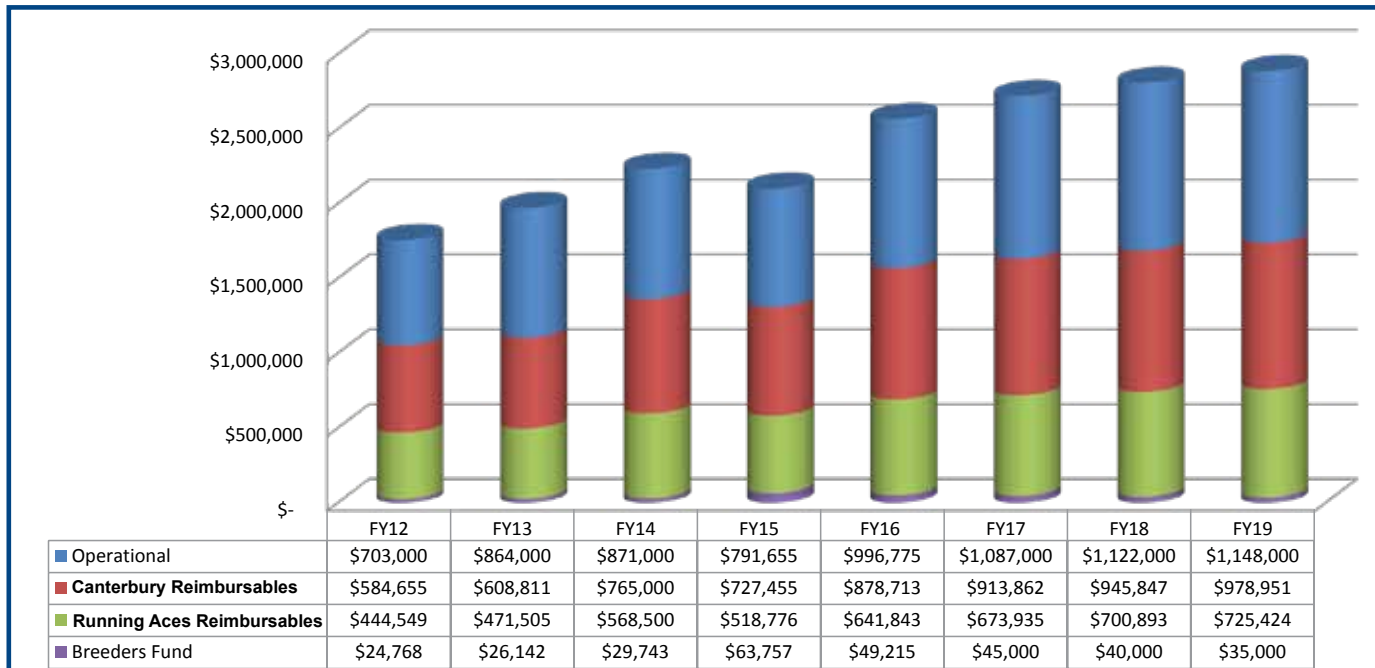
MRC recognizes that the public interest includes ensuring the integrity of horse racing, protecting the health, safety and welfare of racing's human and equine participants, and promoting the racing and breeding industry in Minnesota in order to provide economic stimulus. This report is written with those purposes in mind. Our goal, as always, is to maintain and grow a well-regulated and thriving racing industry. We hope this report will contribute to achieving those ends.

I. THE COST OF REGULATION

For the vast majority of the racing industry’s existence, the industry has paid for its own regulation. Without new sources of revenue, the increased cost of proper oversight will put additional pressures on an industry that is currently only able to obtain marginal profits. The current single source of money to pay for the MRC’s operational expenses is licensing

fees, which have remained stagnant at approximately \$825,000 annually. Even with increased license fees of approximately \$100,000 being requested in the next fiscal year (FY17), the agency will still have a shortfall of \$420,000 in the next biennium, which is within \$50,000 of the shortfall covered by the General Fund appropriation this biennium.

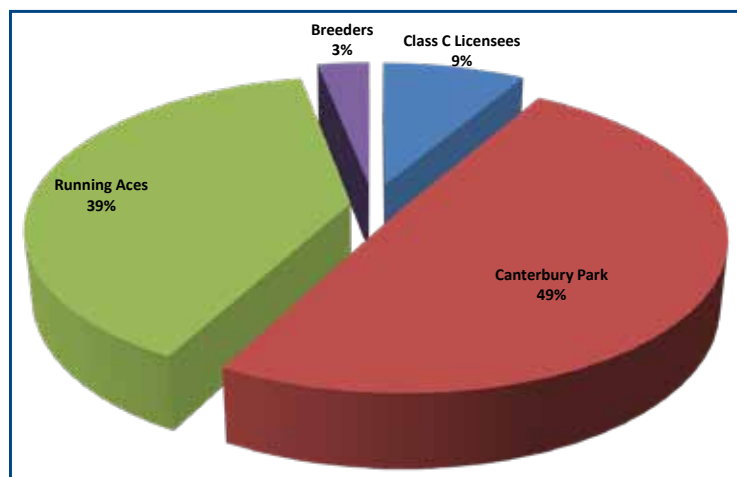
COST OF REGULATION OF HORSE RACING AND CARD ROOM ACTIVITIES



- The expenditures of the Minnesota Racing Commission are divided into three categories:**
1. An operational budget which covers all expenditures associated with oversight of horseracing, excluding veterinarian services, stewards and judges’ contracts, and the medical/drug testing of horses (MS 240.155)
 2. Two reimbursable budgets paid by the racetracks, which cover the aforementioned excluded items and all expenditures associated with the oversight of card room operations (MS 240.30, subd. 9)
 3. A budget for expenditures associated with the administration of the Minnesota Breeders Fund

SOURCE OF FUNDING FY15

As this chart denotes, 88% of the cost of regulation is being paid directly by the racetracks. Even in a controlled cost environment, the racetracks will have to find new sources of revenue to offset over \$240,000 of projected increases in regulation costs next biennium.



II. ECONOMIC IMPACT OF THE RACING INDUSTRY IN MINNESOTA

In Minnesota, there is no recent analysis of the full economic impact of the State’s racing and equine industry. Policymakers, and the industry itself, have no true measure of the industry’s size and importance. What is certain is that the equine industry, and in particular the racing and breeding sector, is a significant contributor to many sectors of the Minnesota economy.

The direct and indirect economic impacts are far ranging in the leisure and entertainment, travel and tourism, agricultural, professional and trade labor, and construction segments of our economy. The racing industry generates thousands of jobs. It brings people here from all over the country, and from other countries, who spend their summers (and their wages) in Minnesota. The industry is a multi-level workforce employer with positions ranging from low-skill to professional, from race track “backside” employees such as grooms and farriers to professionals in veterinary medicine, farm management, and racetrack operations. The industry is environmentally responsible. It leaves the landscape in a healthy condition and contributes to the preservation of open space. The racetracks themselves play an important role in the leisure and hospitality sector. Apart from Twins games, there is almost no other venue in the Twin Cities that attracts more patrons during the summer months than the two race tracks. And, importantly, it is relatively inexpensive to regulate with virtually no cost to regulate the breeding industry and little cost--compared to other industries-- to regulate pari-mutuel racing. In short, it is an industry worth fighting for.

As noted, little research has been done to document these economic impacts and their multiplier effects throughout our state. By contrast, other states have conducted economic impact analyses in the recent past. These studies provide a useful measure in that some of these states have racing industries similar to Minnesota’s when measured by number of tracks, pari-mutuel handle, size of breeding operations and the like.

--In 2014, the Delaware Department of Agriculture reported that the Delaware racing industry’s total economic contribution was \$121 million.

--In 2014, the West Virginia Bureau of Business and Research concluded that the Thoroughbred and greyhound racing industry contributed \$321 million in total business volume to the West Virginia economy. This included 12 percent of the state’s leisure and hospitality sector, 7300 jobs, \$100 million in employee compensation, and \$4.6 million in state tax revenue.

--In 2014, Arkansas reported that the two racing venues in that state--one Thoroughbred and one greyhound--contributed \$895 million to the state’s economy in 2012.

Other states, including New Jersey and Kentucky, have conducted government-sponsored economic impact studies that show impacts of more than \$1 billion in those states.

MRC recommends that the State sponsor and fund an economic impact analysis of the racing industry’s impact on the Minnesota economy so as better to inform legislators in shaping public policy.



III. STATE OF THE INDUSTRY

The people of Minnesota are known for their Midwestern values--a strong work ethic, entrepreneurship, and environmental responsibility. Those same characteristics permeate throughout the racing community. There exists within this community an unwavering devotion to the health, welfare and safety of the horse and an awe for the majestic nature of the equine athlete. Minnesota's racing industry adheres to the highest standards of care for race track safety and has been recognized as an industry leader in that regard. (Canterbury Park was fully re-accredited in 2014 by the National Thoroughbred Racing Association's Safety and Integrity Alliance. The Alliance uses a Code of Standards to audit for compliance with safety standards and racing integrity.) Canterbury Park and Running Aces are among the cleanest, safest, most family-friendly race tracks in the United States.

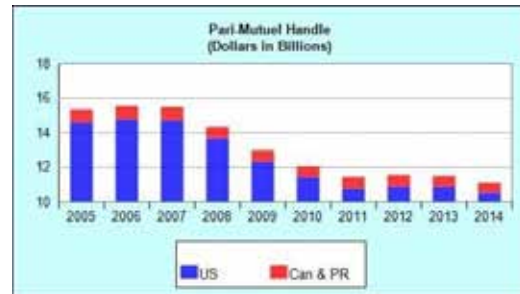
Race track managements at both Canterbury Park and Running Aces have invested heavily in their respective venues. In just the last two years, the tracks have invested millions in capital improvement projects. In 2014, the tracks combined to spend over \$4 million in marketing horse racing and hosting special events. The tracks are leaders in their communities in charitable giving and support of community programs.

Despite these efforts, and despite the positive impact on the state's economy, the horse racing industry in Minnesota (and, indeed, nationwide) faces unprecedented challenges which, if addressed with a proper sense of urgency and with the same mindset that has been applied to any of the many other Minnesota sports and entertainment-related challenges, can turn these challenges into opportunities. But the consequences of ignoring the difficulties faced by the industry could be severe and irreversible.

These challenges essentially fall into four broad categories--declining industry trends; competition from other states; competition from other forms of gaming; and a business model created by statute for the racing industry and the regulatory authority that has become obsolete over time. Competition for the gaming dollar from within and outside the state has been well-documented elsewhere. Therefore, this report discusses the first and last of these challenges.

A. Industry Trends

Indicators of the health of the horse racing industry on a national level suggest that the industry is struggling in spite of efforts by racetrack management, organizations representing horse owners and breeders, state regulators and Legislatures to reverse the trend. Whether measured by pari-mutuel handle (the total amount of all wagers), size of foal crop, or number of races--all key indicators of industry health--the trends are significantly downward. As shown below, total reported pari-mutuel handle on horse racing in the United States has steadily declined from approximately \$15 billion in 2002-2004 to less than \$11 billion in 2014.



Pari-Mutuel Handle

| Year | UNITED STATES* | | Total | % Change | CANADA* | | Total | PUERTO RICO* | | Total | Total* |
|------|----------------|-----------|--------|----------|----------|-----------|-------|--------------|-----------|-------|--------|
| | On Track | Off Track | | | On Track | Off Track | | On Track | Off Track | | |
| 1990 | - | - | 9,385 | 1.1 | - | - | 823 | - | - | - | 10,208 |
| 1991 | - | - | 9,393 | 0.1 | - | - | 804 | - | - | - | 10,198 |
| 1992 | - | - | 9,639 | 2.6 | - | - | 770 | - | - | - | 10,409 |
| 1993 | - | - | 9,600 | -0.4 | - | - | 731 | - | - | - | 10,331 |
| 1994 | - | - | 9,897 | 3.1 | - | - | 681 | - | - | - | 10,578 |
| 1995 | - | - | 10,429 | 5.4 | - | - | 795 | - | - | - | 11,224 |
| 1996 | 2,944 | 8,683 | 11,627 | 11.5 | 259 | 383 | 642 | 10 | 257 | 267 | 12,536 |
| 1997 | 2,703 | 9,839 | 12,542 | 7.9 | 217 | 310 | 527 | 9 | 249 | 258 | 13,327 |
| 1998 | 2,498 | 10,617 | 13,115 | 4.6 | 188 | 310 | 498 | 7 | 185 | 192 | 13,805 |
| 1999 | 2,359 | 11,365 | 13,724 | 4.6 | 161 | 278 | 439 | 7 | 238 | 245 | 14,408 |
| 2000 | 2,270 | 12,051 | 14,321 | 4.4 | 150 | 325 | 475 | 10 | 236 | 246 | 15,042 |
| 2001 | 2,112 | 12,487 | 14,599 | 1.9 | 153 | 387 | 540 | 8 | 208 | 216 | 15,355 |
| 2002 | 2,029 | 13,033 | 15,062 | 3.2 | 153 | 414 | 567 | 8 | 221 | 229 | 15,858 |
| 2003 | 1,902 | 13,278 | 15,180 | 0.8 | 139 | 397 | 536 | 8 | 218 | 226 | 15,942 |
| 2004 | 1,860 | 13,239 | 15,099 | -0.5 | 137 | 364 | 501 | 8 | 228 | 236 | 15,836 |
| 2005 | 1,741 | 12,820 | 14,561 | -3.6 | 144 | 424 | 568 | 8 | 239 | 247 | 15,376 |
| 2006 | 1,688 | 13,097 | 14,785 | 1.5 | 109 | 419 | 528 | 8 | 229 | 237 | 15,550 |
| 2007 | 1,670 | 13,055 | 14,725 | -0.4 | 132 | 375 | 507 | 8 | 206 | 214 | 15,446 |
| 2008 | 1,489 | 12,173 | 13,662 | -7.2 | 96 | 393 | 489 | 7 | 188 | 195 | 14,346 |
| 2009 | 1,325 | 10,990 | 12,315 | -9.9 | 87 | 403 | 490 | 6 | 162 | 168 | 12,973 |
| 2010 | 1,199 | 10,220 | 11,419 | -7.3 | 78 | 425 | 503 | 5 | 149 | 154 | 12,076 |
| 2011 | 1,229 | 9,541 | 10,770 | -5.7 | 73 | 449 | 522 | 5 | 140 | 145 | 11,437 |
| 2012 | 1,239 | 9,643 | 10,882 | 1.0 | 70 | 486 | 556 | 6 | 127 | 133 | 11,571 |
| 2013 | 1,185 | 9,692 | 10,877 | -0.0 | 58 | 431 | 489 | 5 | 113 | 118 | 11,484 |
| 2014 | 1,175 | 9,377 | 10,552 | -3.0 | 56 | 414 | 470 | 4 | 94 | 98 | 11,120 |

* Dollars in millions

Note: There was a \$9 million reconciliation (.085%) in total handle for 2010.

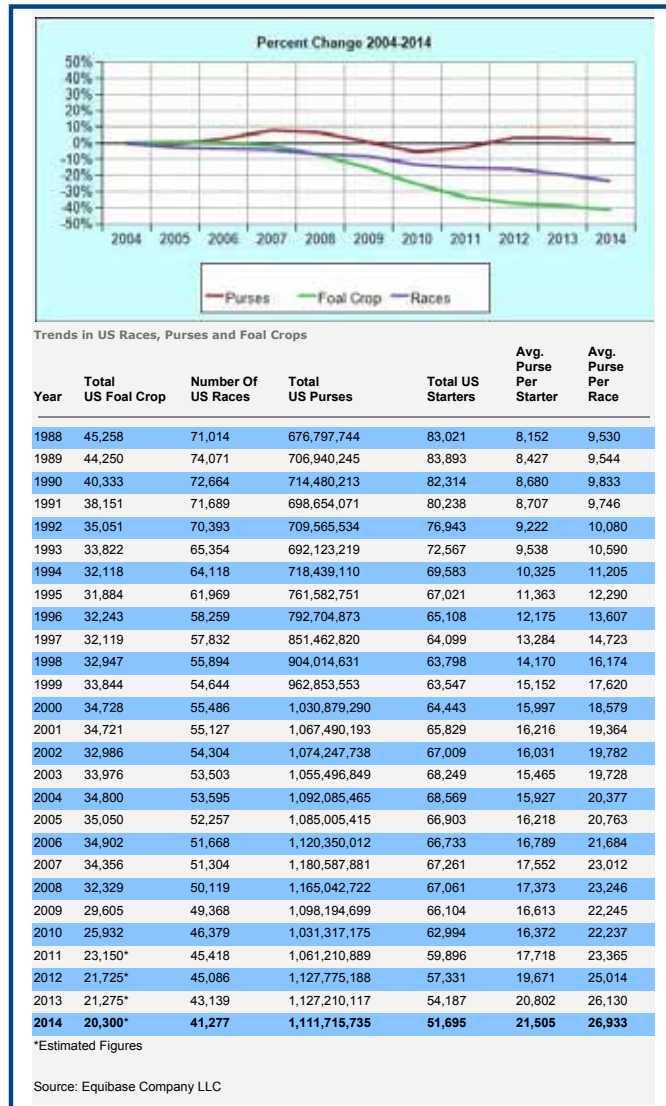
Wagering totals for the U.S., Canada and Puerto Rico include wagering from all sources on race days with at least one Thoroughbred race as reported to Equibase.

In some instances, totals may not equal the sum of on-track and off-track figures due to rounding.

Includes worldwide commingled wagers on races in the U.S., Canada and Puerto Rico and separate pool wagering on U.S. races.

Sources: Equibase Company LLC, CHRIMS (Comprehensive Horse Racing Information Management Systems), and Hipodromo Camarero

The projected national foal crop in 2015 is 22,000, steadily declining from a high of over 51,000 foals in 1986. The number of races run has declined from 74,071 in 1989 to just over 41,000 in 2014. These statistics are shown below in the cumulative chart from The Jockey Club.



Notably, total U.S. purse money has remained relatively constant at over \$1 billion since 2000, largely due to purse supplements from alternative forms of gaming to make up for the slide in pari-mutuel handle.

When it comes to individual states, purse structure, number of race days and races offered, and state-bred foal crops are the backbone of a sustainable racing industry. Higher purses attract fuller fields and higher quality horses to compete for those purses, which fuels increases in pari-mutuel wagering, thus providing revenue to the racetracks and incentives to breeders. Trainers and owners follow the purse money. Racing as a business proposition is attractive to industry participants if there are a sufficient

number of racing opportunities with sufficiently high purses to make it worthwhile to race and breed in a particular state. Therefore, it is instructive to look at the trends in Minnesota.

In some respects, the Minnesota racing industry has “outperformed” its counterparts in other states and, in some respects, it has not.

With respect to purses, Thoroughbred and Quarter horse purses at Canterbury Park have increased from \$6 million in 2009 to over \$14 million in 2015. As a result, Canterbury Park now attracts the best quality of racing in the Midwest as its purse structure has increased in both absolute terms and relative to other tracks with which it competes in the summer months. At Canterbury Park, the number of races run has been fairly constant while field size has risen above the national average. However, the purse increases are almost entirely attributable to Canterbury’s innovative purse enhancement and cooperative marketing agreement with the Shakopee Mdewakanton Sioux Community (SMSC), or Mystic Lake, which contributed purse enhancements of over \$6.2 million in 2015 and will contribute annually up to \$7.8 million in 2022, the agreement’s final year. Absent those purse enhancements, earnings derived from handle on live and simulcast wagering, the means by which the statutory framework is designed to yield purse money, have declined significantly.

Canterbury Park’s simulcast handle alone has declined from \$59 million in 2002 to \$31 million in 2014, or over 46%. Based on information from other states where advance deposit wagering is authorized, this decline in live and simulcast wagering is attributable in large part to Minnesotans wagering through ADW accounts. (Advance deposit wagering is a method of pari-mutuel wagering in which a person may deposit money into an account established with an ADW provider and use the account balance to pay for pari-mutuel wagers. The results are credited or debited to the account holder.)

Running Aces, Minnesota’s only Standardbred track, has not enjoyed the benefit of purse supplements from other than the statutorily-created card rooms and, as such, is not so favorably positioned. The chart below shows average daily purses and purse amounts per race relative to other harness tracks in the country. Running Aces is projected to fall into the

| Rank | State | Track | Live Race Dates | Races | Total Purses | Avg. Purse/Race | Notes |
|------|-------|--------------------------|-----------------|-------|--------------|-----------------|---|
| 1 | NJ | MEADOWLANDS | | 81 | 1047 | \$29,480,986 | \$28,158 |
| 2 | KY | THE RED MILE | | 24 | 324 | \$7,920,421 | \$24,446 Recently Added Historical Racing |
| 3 | NY | YONKERS RACEWAY | | 232 | 2850 | \$55,201,141 | \$19,369 Racino |
| 4 | PA | MOHEGAN SUN POCONO | | 139 | 1980 | \$30,638,725 | \$15,474 Racino |
| 5 | PA | HARRAH'S PHILADELPHIA | | 150 | 2093 | \$32,133,419 | \$15,353 Racino |
| 6 | OH | SCIOTO DOWNS | | 90 | 1138 | \$15,850,724 | \$13,929 Racino |
| 7 | IN | HOOSIER PARK | | 160 | 2164 | \$28,618,363 | \$13,225 Racino |
| 8 | PA | THE MEADOWS | | 208 | 3108 | \$36,933,108 | \$11,883 Racino |
| 9 | DE | DOVER DOWNS | | 105 | 1575 | \$17,728,504 | \$11,256 Racino |
| 10 | NY | TIOGA DOWNS | | 61 | 704 | \$7,531,356 | \$10,698 Racino |
| 11 | MI | HAZEL PARK RACEWAY | | 10 | 118 | \$1,027,300 | \$8,706 Only 10 days of Racing/Year |
| 12 | DE | HARRINGTON RACEWAY | | 84 | 1140 | \$9,588,724 | \$8,411 Racino |
| 13 | IL | BALMORAL PARK | | 114 | 1233 | \$10,348,222 | \$8,393 Permanently Closing 12/31/15 |
| 14 | NY | VERNON DOWNS | | 90 | 968 | \$7,660,556 | \$7,914 Racino |
| 15 | NY | SARATOGA HARNES | | 160 | 2000 | \$15,554,279 | \$7,777 Racino |
| 16 | FL | POMPANO PARK | | 116 | 1124 | \$7,149,356 | \$6,361 Racino |
| 17 | NY | BATAVIA DOWNS | | 70 | 843 | \$5,279,668 | \$6,263 Racino |
| 18 | NY | BUFFALO RACEWAY | | 96 | 1133 | \$6,975,760 | \$6,157 Racino |
| 19 | MD | ROSECROFT RACEWAY | | 54 | 667 | \$4,076,208 | \$6,111 |
| 20 | MD | OCEAN DOWNS | | 48 | 519 | \$2,938,284 | \$5,661 Racino |
| 21 | MI | NORTHVILLE DOWNS | | 10 | 116 | \$649,200 | \$5,597 Only 10 days of Racing/Year |
| 22 | IL | MAYWOOD PARK | | 78 | 937 | \$5,075,729 | \$5,417 Permanently Closed 11/1/15 |
| 23 | MN | RUNNING ACES HARNES | | 53 | 473 | \$2,558,523 | \$5,409 |
| 24 | OH | HOLLYWOOD DAYTON RACEWAY | | 57 | 737 | \$3,958,993 | \$5,372 Racino opened in 2015 |
| 25 | OH | MIAMI VALLING RACING | | 65 | 736 | \$3,780,396 | \$5,136 Racino opened in 2015 |
| 26 | OH | NORTHFIELD PARK | | 213 | 3192 | \$16,276,089 | \$5,099 Racino opened in 2015 |
| 27 | VA | COLONIAL DOWNS | | 24 | 250 | \$1,266,333 | \$5,065 Permanently Closed 10/1/14 |
| 28 | NJ | FREEHOLD RACEWAY | | 108 | 1189 | \$5,477,095 | \$4,606 |
| 29 | ME | SCARBOROUGH DOWNS | | 102 | 956 | \$4,117,011 | \$4,306 |
| 30 | NY | MONTICELLO RACEWAY | | 201 | 2009 | \$7,312,571 | \$3,640 |
| 31 | ME | BANGOR RACEWAY | | 54 | 506 | \$1,768,282 | \$3,495 Racino opened in 2015 |
| 32 | MA | PLAINRIDGE RACECOURSE | | 80 | 736 | \$2,468,042 | \$3,353 |
| 33 | CA | CAL-EXPO | | 60 | 783 | \$2,617,036 | \$3,342 |
| 34 | MI | SPORTS CREEK RACEWAY | | 11 | 145 | \$418,794 | \$2,888 |
| 35 | KY | THUNDER RIDGE RACING | | 21 | 110 | \$198,380 | \$1,803 |
| 36 | KY | PLAYERS BLUEGRASS DOWNS | | 15 | 113 | \$193,635 | \$1,714 |

bottom quartile in the U.S. for 2016 due to enhanced purses in other states driven by approval of casino gaming and other gambling revenue sources. As a result, Running Aces' recent live meets have been characterized by small fields and a lack of growth in live handle.

With respect to foal crops, Minnesota's foal crop for all breeds has declined from its peak in 1989 of 1015 to 359 in 2014. Declining foal crops affect field size, the number of races that can be offered and, eventually pari-mutuel handle and purses, thus creating a cycle of decline. Canterbury Park's rising purse structure is starting to make an impact on breeding crops, but Running Aces' purse structure does not provide the same incentives. Most importantly, foal crops affect Minnesota's agribusiness (the farms where breeding occurs) and the ability of breeders to maintain the infrastructure and personnel required to breed and care for horses.

B. Some Aspects of Minnesota's Model for Regulating the Racing Industry Are Obsolete

Gambling is a government-created monopoly that cannot take place, at least in theory, where it is not authorized. Decisions about what form of gambling to authorize and how it should be regulated are at least as important as advertising and price competition are in other industries. In other words, they define who can reach markets and on

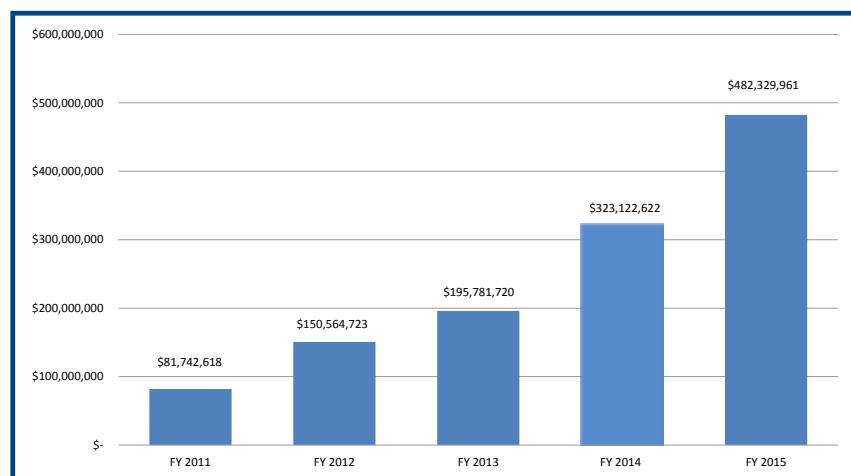
what terms.

Minnesota's race tracks have been largely precluded by state law from distributing their product to Minnesota customers through the primary means by which any industry grows today-- the Internet. In the past, MRC had issued this caveat to Minnesota race track licensees in its annual license approval: "No account wagering, telephone wagering, wagering by personal computer or by an interactive wagering system may be conducted in Minnesota nor may any such wagers placed from within Minnesota be accepted at any location in this or any other state."

This interpretation of the law is not only inconsistent with the Federal Interstate Horse Racing Act, 15 U.S.C. Section 3001 et seq., but it ignores the changing landscape of how people wager on horse races and what is actually enforceable. More important, it places a virtual stranglehold on the ability of Minnesota's racing industry to thrive and grow. In short, times have changed but the law has not.

Today, 88%, or almost \$10 billion of total U.S. pari-mutuel handle, is wagered from locations outside the tracks through simulcast outlets, brick and mortar off-track betting sites (OTB's), and advance deposit wagering hubs (ADW's). Of these, only ADW's are experiencing significant growth. The chart below shows the increases in ADW handle in North Dakota from FY 2011 to FY 2015:

ADW HANDLE BY FISCAL YEAR



The table below, taken from a 2013 economic impact study of the Massachusetts Thoroughbred industry, is even more illustrative of the relative

trends over time in live and simulcast handle versus ADW handle:

Exhibit 7.4: Suffolk Downs Handle 2000-2012

| Year | Number of Live Days | Live Handle | Simulcast Handle | Onsite Handle | Transmitted (Export) Handle | All Sources Handle | ADW Handle | Total |
|------|---------------------|----------------------|-------------------------|------------------------|-----------------------------|------------------------|----------------------|------------------------|
| 2000 | 145 | \$27,555,803 | \$142,214,814 | \$169,770,617 | \$104,861,162 | \$274,631,779 | | \$274,631,779 |
| 2001 | 149 | 24,402,478 | 145,302,304 | 169,704,782 | 101,801,542 | 271,506,324 | | 271,506,324 |
| 2002 | 150 | 24,278,850 | 140,398,788 | 164,677,638 | 138,300,647 | 302,978,285 | | 302,978,285 |
| 2003 | 148 | 21,672,633 | 131,484,948 | 153,157,581 | 136,392,704 | 289,550,285 | 5,778,788 | 295,329,073 |
| 2004 | 119 | 17,347,549 | 128,713,475 | 146,061,024 | 114,535,169 | 260,596,193 | 8,359,317 | 268,955,510 |
| 2005 | 116 | 14,745,024 | 119,613,147 | 134,358,171 | 109,187,183 | 243,545,354 | 12,791,711 | 256,337,065 |
| 2006 | 103 | 11,060,701 | 112,840,486 | 123,901,187 | 82,943,733 | 206,844,920 | 17,096,290 | 223,941,210 |
| 2007 | 100 | 12,270,182 | 104,399,657 | 116,669,839 | 78,113,286 | 194,783,125 | 27,433,318 | 222,216,443 |
| 2008 | 102 | 11,624,781 | 88,582,631 | 100,207,412 | 90,425,446 | 190,632,858 | 30,233,000 | 220,865,858 |
| 2009 | 101 | 9,053,766 | 75,618,350 | 84,672,116 | 99,727,711 | 184,399,827 | 55,346,926 | 239,746,753 |
| 2010 | 101 | 7,833,438 | 69,184,640 | 77,018,078 | 98,435,570 | 175,453,648 | 64,601,024 | 240,054,671 |
| 2011 | 80 | 6,729,713 | 64,626,699 | 71,356,413 | 64,224,602 | 135,581,014 | 64,696,913 | 200,277,927 |
| 2012 | 80 | 6,478,074 | 59,571,017 | 66,049,091 | 69,202,672 | 135,251,764 | 76,716,748 | 211,968,512 |
| | Total | \$195,052,993 | \$ 1,382,550,955 | \$1,577,603,948 | \$1,288,151,427 | \$2,865,755,375 | \$363,054,034 | \$3,228,809,409 |

Note: Live Handle is wagering on live races by patrons at Suffolk Downs; Simulcast Handle is wagering on races at other facilities by patrons at Suffolk Downs; Onsite Handle is the total of Live and Simulcast Handle; Transmitted Handle (Export Handle) is wagering on live races at Suffolk Downs by patrons at facilities outside Massachusetts (including wagering on Suffolk races at Plainridge and Raynham); All Sources Handle is Onsite plus Transmitted Handle; ADW Handle is online wagering by Massachusetts residents through TVG, Xpress Bet, You Bet and Twin Spires. These pools are not maintained by Suffolk Downs;

Source: Suffolk Downs

Exhibit 7.5 presents the data presented in Exhibit 7.4 in line chart format.



The New York State Legislature acted quickly when the New York Racing and Wagering Board found that roughly \$200 million was lost annually by not regulating multi-jurisdiction account wagering providers in similar fashion to in-state providers. The New York Assembly responded by enacting legislation in 2014 to require out-of-state ADW companies to pay regulatory and statutory fees to the state and industry participants such as horsemen and breeders. The New York Assembly declared that “like other states, in enacting this legislation New York will be protecting its own racing industry.”



Minnesota’s restriction of pari-mutuel racing to the premises of a licensed race track is both unenforceable and out of step with federal law and the laws of almost every other racing state. The federal Interstate Horse Racing Act, as amended in 2000, authorizes remote wagering on horse races. As a result, the majority of states allow residents to wager using electronic devices across state lines through licensed ADW providers. Such wagering is taking place today by Minnesota residents through ADW providers who are not licensed by the MRC, although those account holders are presumably “blocked” by ADW providers from wagering on races at Minnesota’s tracks. The net result of this obsolete legal framework is that the Minnesota racing industry and the state have lost hundreds of millions of dollars in pari-mutuel handle by forcing it out of state to other (competing) tracks. Minnesota’s race tracks, owners and breeders have lost revenues and the Minnesota racing industry has been placed on an uneven footing with its counterparts in other states.

ADW wagering is so woven into the fabric of today’s racing world that people wager through their ADW accounts while at the track, further depriving the track of its statutory share of live racing and simulcast handle. Casual fans and infrequent visitors may stand in line to wager with a live pari-mutuel clerk, but experienced and high volume players wager through their electronic devices both for the convenience and for the edge provided by betting late into a pool when the odds are certain. ADW account wagering has become so common that Groupon now offers coupons for wagering credits. The growth of ADW activity is likely to continue given horseplayers’ desire for convenience and the advancements in streaming mobile video. People can “play the horses” anytime and anywhere.



IV. GUIDING PRINCIPLES

The MRC believes that some guiding principles should apply in evaluating funding alternatives. Those principles are as follows:

1. The MRC should have a secure and dedicated funding source that allows it to ensure proper oversight of racing, pari-mutuel wagering and card playing activities at the licensed race tracks.

In order for racing to thrive, the public must have absolute confidence in the integrity of the sport. In recent years, the MRC has been understaffed and underfunded both relative to other states' racing commissions and in absolute terms. Moreover, its human resources have not always been properly aligned with its mission. As a result, prior Office of Legislative Auditor's (OLA) reports have found deficiencies in MRC's oversight of card room activities and purse contributions.

The MRC's current leadership has addressed these deficiencies through tighter operational and accounting controls and new hires, while not increasing the size of the staff. The 2015 OLA report found MRC to be compliant with all internal and accounting control requirements.

2. Various participants in the industry should share in the funding of the regulatory body and that cost burden should be fair and proportional.

Everyone in the industry has an interest in promoting its integrity and success. In Minnesota, as in many states, the cost burden falls heavily and

disproportionately on the licensed race tracks. This is made evident in the chart in Section I.

However, there are a number of essentially "free riders" who enjoy the benefits of participating in the Minnesota racing industry but do not pay their fair share. In addition to ADW providers--whose free riding is described above--these include gaming vendors, totalizator companies and others whose activities are at the core of maintaining the integrity of pari-mutuel wagering and gaming operations but who pay little for the privilege of doing business in Minnesota due to a statutory ceiling on license fees that existed from 1983 until 2015. The Legislature's removal of the \$100 license fee cap on occupational licensees (which includes vendors) in the 2014-15 Legislative session will help rectify this imbalance.

3. Given the beneficial economic impact of the racing industry in Minnesota and the importance of maintaining its integrity, the State should share in the responsibility for funding the MRC.

A substantial portion of MRC's operating budget is made up of charges from other state agencies. In fact, costs passed on to MRC from other agencies were \$261,000 in FY 2014, thereby exceeding the \$199,000 in total revenue that MRC derived from licensing all 5500 occupational licensees. These other state agencies are essential to MRC's core activities of processing licenses and enforcing the law, but at the same time the cost of these services places additional pressures on MRC's budget.



V. FUNDING ALTERNATIVES FOR MRC

The first two funding sources--players and race tracks--follow the traditional formula of imposing costs on industry participants to self-fund regulatory oversight. These options are included to foster discussion but each of them adds to the industry's cost burden without any possibility of spurring growth.

1. Players

--Increase the statutory takeout rate set forth in Minn. Stat. 240.13, subd. 4 by .125% to .5% on some or all types of parimutuel wagers.

"Takeout" means the total amount of money, excluding breakage, withheld from each parimutuel pool, as authorized by statute or rule. The current takeout rates are 17% and 23% depending on the type of wager. Increasing the takeout by a fractional amount would keep Minnesota's takeout rate within the mid-range seen in other states and could net from \$50,000-\$200,000 per year. However, increasing takeout rates goes against the industry trend to reduce rates in the belief that reductions stimulate increased pari-mutuel wagering.

2. Race Tracks

--Increase the statutory annual license fees in Minn. Stat. 240.10 and/or expand the scope of the reimbursement account set forth in Minn Stat. 240.155 to include costs related to investigations and increased enforcement activities.

Under Chapter 240, the race tracks pay both an annual license fee and reimburse the MRC for certain direct costs related to horse racing (veterinary expenses, medication testing) and oversight of the card rooms. The amounts of these "reimbursables" are shown at the beginning of this report. The reimbursement account could be expanded to include the direct costs for background checks of license applicants and investigations related to drugs or other racing violations, all of which are key elements of ensuring a level playing field for racing participants and protecting public health, welfare and safety.

Given that the race tracks already provide an overwhelming majority of MRC's financing, this is an unattractive option because it merely shifts more costs from the state to the race tracks at a time when both tracks need increased revenue to grow.

--Dedicate a portion of the "breakage" and unclaimed winning tickets currently retained by the race tracks to the MRC.

"Breakage" is a rounding mechanism to deal with odd cents of all money wagered when payoffs are made to winning ticket holders. In Minnesota, there is an imposed tax of 6% of the amount in excess of \$12 million annually on takeout, including breakage, in any fiscal year. Minn. Stat. 240.15, subd. 1. This threshold has never been reached. Therefore, under the statute, the tracks have the right to retain all breakage and winning tickets that go unclaimed for 12 months. In FY 2014, these amounted to over \$400,000. Some states apportion these revenues among the tracks, horse persons' associations and the state, or combinations thereof. Directing a portion of these funds to the MRC would require statutory change.

The following option--direct contribution of funds from the State--is based on the third guiding principle, which is that the State of Minnesota has a major stake in ensuring that racing is conducted in the public interest and continues to generate state-wide economic benefit.

3. State of Minnesota

--Dedicate a portion of the approximately \$1 million in state sales taxes paid by race tracks to the MRC.

This would essentially be a "user fee" on patrons of the tracks who enjoy the benefits of well-regulated racing and card playing. There is precedent for such an approach in Minn. Stat. 297A.94 and in the many other taxes imposed for special purposes, such as stadium construction and the like. It would be a secure and dedicated source of funding that maintains the "closed-loop" system of having industry participants, in this case track patrons, fund the MRC.

--Redirect fine revenue under Minn. Stat. 240.22 from the general fund to a beneficial purpose such as racehorse retirement and rescue.

Total fine revenue from MRC enforcement typically ranges from \$35,000-50,000 annually and could be reinvested into the industry for the benefit of those who “play by the rules.” The MRC spends substantial time and resources on enforcement, including Attorney General costs. While use of fines for the MRC’s operational budget could pose a conflict of interest, dedicating those receipts to a beneficial racing-related purpose seems a better use than the trifling contribution these funds make to the general fund. This would require amending Minn. Stat. 240.22.

--Reconsider appropriation of general funds to MRC in light of the importance of maintaining a well-regulated racing industry and to relieve the burden of increasing regulatory costs on the industry itself.

4. Gaming Vendors and Tote Companies

--Increase license fees for gaming vendors and totalizator (tote) companies to reflect the true costs of licensing, regulatory oversight and risk management.

Gaming vendors are those persons and entities that manufacture or distribute gaming-related equipment or provide gaming-related services to card rooms and whose products or services are directly related to or affect the outcome of card games. These vendors require extensive background checks and are critical to the integrity of the card room games. License fees in other states for such vendors far exceed those in Minnesota, where license fees have previously been capped at \$100. MRC intends to promulgate a rule to increase gaming vendors’ annual license fees to bring them into line with “market rates” in other jurisdictions. Under Minn. Stat. 240.03, subd. 10, legislative approval will be required for these changes, which were built into MRC’s FY 2017 budget forecast.

Tote companies, provide the system by which pari-mutuel activity, including buying and selling tickets and displaying pari-mutuel information, is

accomplished through the system’s link to a central processing unit. Tote companies play an important role in protecting the betting public’s and the State’s interests. The security and reliability of tote systems are essential to the prevention of pari-mutuel problems, such as wagering fraud, past posting, odds manipulation and money laundering, and to the daily monitoring and accurate reconciliation of taxes, takeout, payoffs and payments between tracks that send and receive each other’s signals. Again, license fees will be increased, subject to legislative approval, to reflect the true costs of regulation and the risks that a tote malfunction can present to the integrity of pari-mutuel wagering.

5. Advance Deposit Wagering (ADW) Companies

--The Legislature should expressly authorize advance deposit wagering in Minnesota and the MRC should license and regulate ADW providers to ensure the integrity of pari-mutuel wagering in Minnesota.

Most states that have pari-mutuel statutes permit advance deposit account wagering and require ADW operators to secure a license from the state regulatory body having jurisdiction over horse race wagering in the state. Typically, ADW operators must meet certain requirements as a condition of accepting wagers in the state. Those requirements may include contracting with an in-state licensed track and obtaining approvals of the contract from the horse persons’ association and the racing commission, payment of “source market fees” to the in-state race track, or payment of specified taxes and fees to the state for redistribution to the tracks, horse persons’ associations and regulatory authority.

Minnesota’s failure to license and regulate ADW providers has allowed these wagering platforms to essentially poach customers from Minnesota race tracks without providing much-needed revenues to the MRC, the tracks, breeders and owners. Wagering by Minnesota residents through ADW providers has essentially pushed that revenue out of Minnesota and into other states, to the benefit of their race tracks, breeders and owners. Lastly, a regulatory framework that fails to regulate such a broad and growing swath of activity that falls within its statutory mandate threatens to undermine the credibility of and trust in the regulatory authority.

Therefore, Chapter 240 should be amended so as to deem pari-mutuel wagers placed with licensed ADW providers under agreements with the licensed race track, which agreements have been approved by the horsepersons' associations and the MRC, to be wagers placed at the track.

6. Other Revenue-Producing Possibilities

As noted above, all forms of gaming have been transformed by innovative technologies, internet access, and new target audiences. The same is true for horse racing. Other states have used these developments to create opportunities for revenue to boost purses, develop fan interest and fund their racing commissions. Examples are lottery games based on horse racing, historic racing (whereby patrons can place bets into live wagering pools on reruns of previously run horse races) and, most recently, fantasy sports wagering.

The MRC will continue to monitor these and other potential sources of revenue enhancement as they are put in place by other states, particularly by those states with which Minnesota competes for racing industry participation. Where suitable for Minnesota, the MRC will work with industry stakeholders in an open process to determine the necessity for legislative or regulatory action.

CONCLUSION

Since racing was authorized in Minnesota in 1983, it has proven to be a resilient industry. It rebounded from the “dark days,” of the early 1990’s when parimutuel racing ceased to exist in Minnesota. It survived the “Great Recession” of the last decade. And today, thanks to the efforts of many, its strengths far outweigh its weaknesses. It is a dynamic industry. In that regard, it is no different from any other industry. Therefore, it is unrealistic to believe that revenue enhancement and growth can be spurred absent significant change and innovation.

In MRC’s 2014 Annual Report, Chairman Ralph Strangis stated that the Commission “needs to be supportive of efforts that will promote industry growth and enhance opportunities for those

who participate in and benefit, both directly and indirectly, from Minnesota racing.” He referred to “untapped opportunities” that could “enhance the economic benefits to the industry and the State.” The Commission has been watching reform developments in other states for the value they might bring to Minnesota’s racing industry and has indicated it will support any initiative that is consistent with its enabling statute and the State’s economic interests. Some of these initiatives may require modest changes in statute or rule to implement. The Commission intends to proceed collaboratively, transparently and through a consensus-building process to create an environment that encourages investment of capital and industry growth.

We hope this report provides a context for thoughtful discussion of how to fund the MRC while helping to spur industry growth. Minnesota’s racing industry is at a crossroads in many respects. Absent modernization of Chapter 240 and other needed changes described in this report, it will continue to face built-in limits on its growth. On the other hand, if the state is willing to give it a “leg up,” Minnesota racing has the potential to catapult into the upper tier on the national racing scene.

We appreciate the opportunity to submit this report and look forward to engaging in a dialogue with the executive and legislative branches about the path forward.

Respectfully submitted,

Thomas DiPasquale
Executive Director
on behalf of and with
the authority of the





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