RECOMMENDATIONS

FOR THE

50^{TH} ANNUAL HORSERACE BETTING LEVY SCHEME

THE 50TH LEVY SCHEME

RECOMMENDATIONS BY THE BOOKMAKERS' COMMITTEE

1 EXECUTIVE SUMMARY

1.1 Bookmakers' total contribution to racing does not justify the current levy.

1.2 Racing's income is rapidly moving to a commercial basis via its increasing charges for media rights and therefore cannot expect levy support to continue at its current level.

1.3 The Bookmakers Committee recommends to the Horserace Betting Levy Board a reduction in the levy for the 50th Levy Scheme.

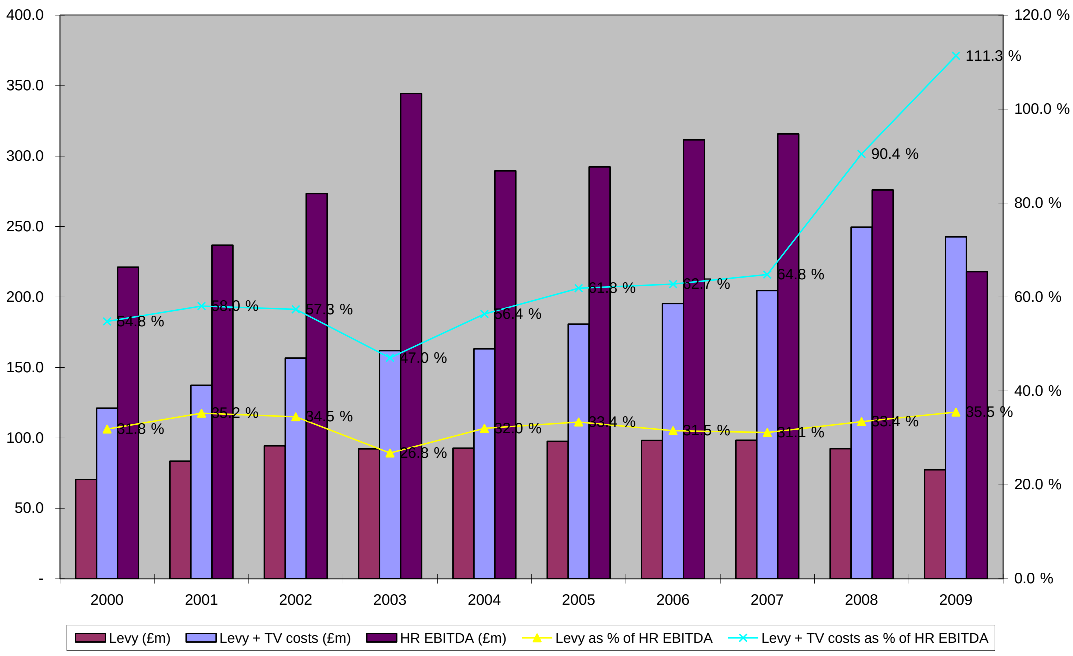
1.4 This should be achieved by increasing the threshold at which Licensed Betting Offices (LBOs) pay the headline rate of 10% of gross profits to £123,000.[1]

1.5 The increase in threshold would be at a cost to the levy of approximately £8.5M. This amount equates to 25% of the additional cost to LBOs and 50% of the additional revenue received by racing each year as a result of increased media charges, FY07/08 to FY09/10.

1.6 We put this forward for three reasons:

1.7 First, the cost of levy and total TV costs now exceeds bookmakers' EBITDA on British horseracing. (**Figure 1)**

Figure 1 Levy as a Share of Bookmakers' British Horserace Betting EBITDA.[2]



[1] Derived from HBLB returns for the 48th Levy Scheme (Annex A).
[2] 50th Horserace Betting Levy Scheme 'Report for The Bookmakers' Committee', E&Y, 8th July 2010.

1.8 Second, the capacity of bookmakers to pay has been reduced as a result of

1.8.1 accelerating decline amongst betting shop customers in betting on British horseracing, resulting in an absolute fall in bookmakers' revenue from betting on British horseracing from 2008 to 2009.

1.8.2 the additional cost (since 1st January 2008) of providing TV pictures into LBOs, and the prospect of further substantial increases in cost from January 2011, before the start of the 50th levy year.

1.8.3 economic conditions that are difficult currently and uncertain in the near future resulting in:

(a) reduced disposable income for the consumer.

(b) a budget that included VAT of 20% from 4th January 2011, further reducing disposable income but increasing bookmakers' costs (including media rights) that are subject to VAT.

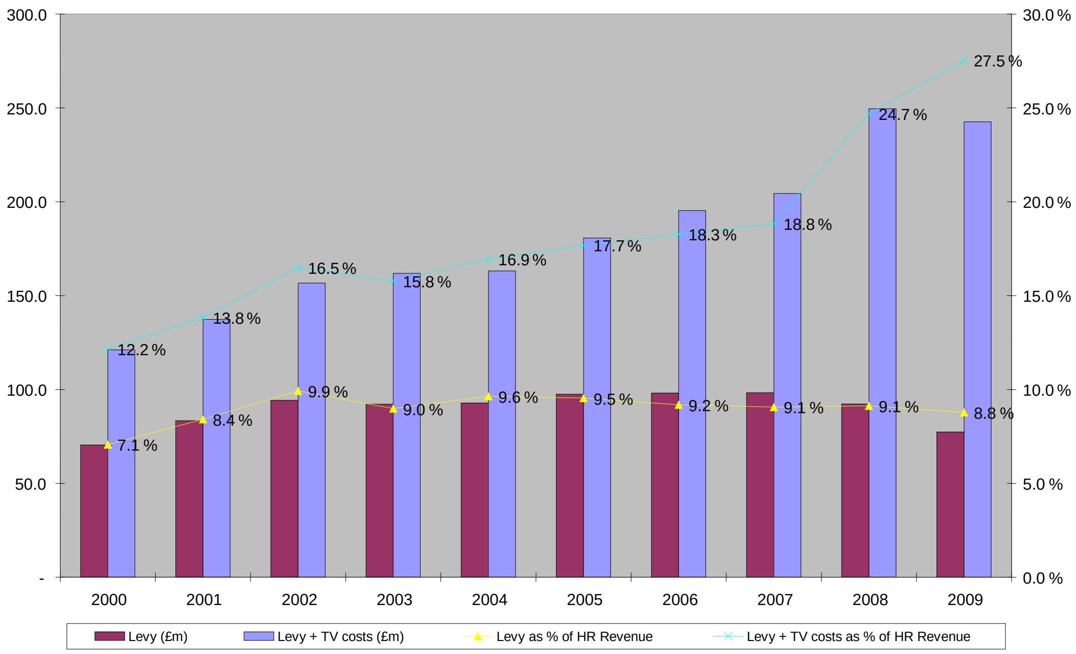
1.9 The net effect of these factors is

1.9.1 turnover has reduced by 6.8%.[3]

1.9.2 gross win has reduced by 18.6%.[4]

1.10 Third, British betting operators, and in particular LBO operators, now pay more in levy and media rights than ever before. The amount of bookmakers' horseracing revenue spent in this way has reached 27.5%. **(Figure 2)**

Figure 2 Levy as a Share of Bookmakers' British Horseracing Betting Revenue.[5]



[3] Memo to ABB Industry Model Steering Group, RS Business Modelling, 7th June 2010.
[4] Ibid.
[5] 50th Horserace Betting Levy Scheme 'Report for The Bookmakers' Committee', E&Y, 8th July 2010.

1.11 For the period 2006-9, racing received from bookmaking £565M excluding sponsorship.[6]

1.12 Racing's needs can and ought to be met from all income sources, not just levy.

1.13 We make this proposal because an increased threshold will

1.13.1 preserve employment in an industry employing over 40,000 people.[7]

1.13.2 limit the number of lower turnover shops likely to close. Media rights are fixed costs and thus affect medium and low turnover shops most.

1.13.3 help to maintain levy contributions by keeping shops open.

1.13.4 reduce the structural competitive advantage of those bookmakers not paying levy, and help arrest the decline of leviable betting on horseracing.

1.13.5 ameliorate the cost implications of those who directly fund the extra £56.1M now received by racing over and above the levy.[8]

1.13.6 maintain the incentive to both racing and LBOs to maximize the potential of British horserace betting.

1.13.7 maintain revenue streams to HMG through VAT, GPT and licence fees.

[6] Satellite Information Services Ltd
[7] An Economic Impact of the British Betting Industry, Deloitte, January 2010.
[8] Satellite Information Services Ltd

2 INTRODUCTION

2.1 The Bookmakers' Committee recognises the efforts made by the Board in attempting to modernise the levy process and generate more time for a decision to be reached internally, with a view to avoiding the necessity for a determination to be made by the Secretary of State.

2.2 The Bookmakers' Committee is pleased to submit its recommendations for the 50th Levy Scheme, per its statutory responsibility, mindful that this is earlier in the year than has previously been the norm.

2.3 The Bookmakers' Committee makes its recommendations for the 50th Levy Scheme in the full knowledge that a determination by Government would be unhelpful for both the betting and racing industries; prolonging the uncertainty that comes from a failure to agree on a scheme and the consequent inability to plan for the 50th Levy Scheme year.

2.4 The context in which the Committee has arrived at its recommendations has changed markedly since agreeing the 49th Levy Scheme.

2.5 The context is different in that:

2.5.1 there is acceleration in the decline in betting shop customers betting on British horseracing, resulting in an absolute fall in bookmakers' revenue from betting on British horseracing from 2008 to 2009.

2.5.2 driven by substantial increases in media rights payments for British horseracing, the additional cost of providing TV pictures into LBOs, and the prospect of further increases with substantial price rises expected from January 2011, before the start of the Levy Year.

2.5.3 poor economic conditions resulting in:

(a) already reduced disposable income for the consumer.

(b) a budget that included VAT of 20% from 4th January 2011 further restricting consumer spending and increasing bookmakers' costs (including media rights) that are subject to VAT (Betting is an exempt supply for VAT purposes and as such an increase in input VAT rates represents a direct increase in costs).

2.6 The net effect of these factors is

2.6.1 turnover reducing by 6.8%.[9]

2.6.2 gross win reducing by 18.6%.[10]

2.7 Racing has continued to receive increased levels of revenue from bookmakers levy and media rights despite the falling value of betting on British horseracing.

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[9] Memo to ABB Industry Model Steering group, RS business Modelling, 7th June 2010.
[10] Ibid.

2.8 Bookmakers' total contribution to racing does not justify a levy at current levels.

2.9 The continuing decline in the popularity of betting on British horseracing, the cost of providing live TV pictures, other relevant costs in LBOs and prevailing economic conditions, justify fully a reduction in the levy.

2.10 This submission shall incorporate expert economic advice obtained from among others, *Ernst & Young*, and *London Economics.* Reports provided to the Bookmakers' Committee shall be made available to the Board when finalised.

3 ORIGINS OF THE LEVY, ITS BACKGROUND AND CONTEXT

Origins

3.1 The Horserace Betting Levy was established under the Horserace Betting Levy Act, 1961 following the legalisation of off-course cash betting. The intention at the time was that the levy would compensate racing for an anticipated loss of attendance at racecourses following the introduction of high street licensed betting offices.

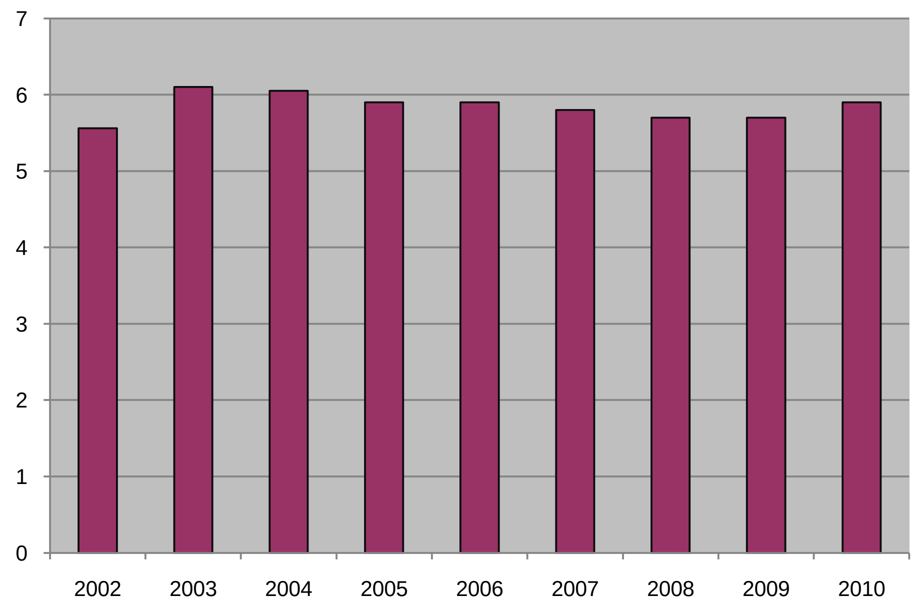
3.2 During the passage of the Levy Act, the Home Secretary, Mr R A Butler, emphasised that the levy was not intended to subsidise individual racehorse owners through the transfer of the public's money from one section of the community (punters) to another (owners). The point of the levy, Mr Butler said, was not to benefit any sectional interest, but to enable a great national sport and a great national industry to help itself.

3.3 The Peppiatt Report,[11] which laid the ground for the Horserace Betting Levy Act, 1963 stated:

'....we understand that attendances at horse race meetings amount to over 6,000,000 in a year...'

Mindful of the possible margin of error for such a statistic produced as it was, in 1960, **Figure 3** shows that the levy has met this objective.

Figure 3 Total Annual Attendance at Racecourses (Millions).[12]



3.4 Total racecourse attendance for 2009 was 5,718,729 compared with 5,716,656 in 2008. Based on Jan-May 2010, the figure for 2010 is expected to increase further to 5,859,353 (+2.4%).

[11] Report of the Departmental Committee on a Levy on Betting on Horse Races, 11th April 1960.
[12] Source: BHA / RCA / HBLB

Price for a Product

3.5 The philosophy underpinning the levy has been re-stated on a number of occasions, most notably by the then Home Secretary Mr Kenneth Baker in March 1992 when, in his determination of the 31st Levy Scheme (1992/3), he stated:

''The levy was never intended to provide a price for a product. Indeed, it is difficult to see how it could do so.''

3.6 The claim that the levy is, in some way, a price for a product supplied by horseracing to the betting industry was first presented by representatives of the Jockey Club in evidence to the Home Affairs Select Committee, which examined the levy in 1991.

3.7 Mr Baker's comment of the following year was made in the full knowledge of the Jockey Club's position and can be seen as confirmation that, some 30 years after the enactment of the legislation, the levy was still regarded by Government as a compensatory payment.

3.8 It is difficult to imagine why the position for the 50th Levy Scheme would have changed as, in the 18 years since Mr Baker confirmed the status of the levy, no Minister has expressed a conflicting view.

Mechanism v Yield

3.9 The language of the statute instituting the levy sets out the mechanism by which a levy is to be devised and created. It does not refer to a certain sum being paid from bookmaking to racing, and from the start recognises the fluctuating fortunes of competitive markets by reference to the fact that it needs to reflect the capacity of bookmakers to pay.

3.10 This was re-iterated by the Levy Board executive in papers to the Board as recently as 24th June 2010.

3.11 The levy was never intended to be an 'upwards only rent review'.

3.12 Previous spending patterns at the Levy Board may suggest that Members did not understand this and continued to spend beyond their means for too long.

3.13 It is unfortunate that the HBLB finds itself in this difficult position, but it is a problem of its own making. It is wrong for the HBLB to expect bookmakers to rescue it from the effect of the ill-conceived financial planning of the past through an increase to the levy.

3.14 The fact that the levy yield has reduced due to reduced betting on British horseracing with levy-paying bookmakers is not a reason to increase the amount payable by those British bookmakers still subject to levy. That will result in further competitive disadvantage that will drive more custom to overseas bookmakers and to exchanges, with a consequential decline in levy yield.

Basis of Payment

3.15 The basis of levy payments has, since the 41st Levy Scheme, reflected the Government's preference for the gross profits taxation of betting.

3.16 The gross profits mechanism incorporated within every levy scheme since 2002 ensures that the levy paid by bookmakers is a more appropriate reflection of their capacity to do so. Increased profits result in increased levy and vice versa.

3.17 The gross profits tax is a tax on the bookmaker and has enabled the British punter to receive the best value, in terms of total payout, for 40 years; we see no grounds as to why the basis of this should change.

The Principle of 'Capacity to Pay'

3.18 Incorporated in the 1969 Horserace Betting Levy Act was the removal of reference to the capacity of bookmakers to pay, the 1961 Betting Levy Act having required Government-appointed members of the Board in the event of a dispute to consider and compare, inter alia, the needs of racing and the capacity of bookmakers to make contributions.

3.19 Following expressions of concern by the betting industry, an amendment was tabled at the Committee stage of the Bill that introduced the 1969 Horserace Betting Levy Act, the effect of which was to retain capacity to pay as an essential consideration.

3.20 In debate, Mr Elystan Morgan, Under-Secretary of State at the Home Office, assured the House that in exercising the functions conferred on him by the Bill, the Home Secretary would have regard to the capacity of bookmakers to pay and that the bookmakers' guarantee was the Home Secretary's independence, impartiality and his regard to what was reasonable.

Determined Schemes

3.21 During the period 2000-2010, levy schemes have been subject to determination by Government on two occasions:

3.21.1 in 2008, by Gerry Sutcliffe MP, Minister for Sport (47th Levy Scheme);

and

3.21.2 in 2002 by Tessa Jowell MP, Culture Secretary (41st Levy Scheme).

Determination of the 47th Scheme

3.22 The 47th Levy Scheme was referred for determination primarily because of disagreement over whether the capacity of bookmakers to pay levy had been or would be reduced by the considerable increase in the cost of acquiring live TV coverage of horseracing. An offset of the incremental costs was proposed but not accepted.

3.23 The Minister accepted that an argument could be put forward

'that bookmakers subscriptions to the new service constitute a commercially-based flow of money to racing'

and further stated

'I therefore accept that it may have a material effect both on bookmakers' ability to pay and on the needs of racing'.

3.24 At the time, it was said that, because the extra cost was not known, the impact could not be adequately assessed and the Minister stated that

'In time its full economic impact on bookmakers, racecourses and on horseracing generally may become clearer.'

3.25 This impact is now clear and is addressed in Section 4. It is clearly the case that the increasing transfer of funds from bookmakers to racing via media rights should be fully taken into account in any approach to determine the levy.

3.26 The Minister elected to revert to the last time both sides had achieved consensus, that being the 46th Scheme the year prior and directed that it would be rolled over, with adjustments for inflation where appropriate.

3.27 The Minister rejected arguments put forward by racing for an increase in levy.

Determination of the 41st Scheme

3.28 In her determination of the 41st Levy Scheme the Minister introduced a gross profits levy that was

'*wholly consistent with the Government's introduction of a gross profits betting tax and is the fairest and most reliable indication of the bookmakers' capacity to pay'*.

3.29 She stated as her principle ruling that

'*The proposed scheme will be based on a payment by off-course bookmakers of around 9% of their gross profits from horseracing'.*

3.30 She further stated

'*I would now like to encourage the betting and racing industries to develop a modern relationship as business partners and move away from an adversarial approach. This scheme will give them a shared interest in developing their businesses to their mutual benefit. It is, however, clear that the levy system as a whole is flawed, and should not be needed if satisfactory commercial agreements between the parties can be made to work.'*

3.31 The determination introduced the current system of thresholds, at a level for the 41st Scheme of £150,000; this level would now be £190,118.[13] The threshold level was

[13] Source: Ernst & Young (as at May 2010)

reduced to £75,000 in the 42nd Scheme commensurate with the removal of foreign racing from liability to levy. Reinstatement of foreign racing as 'leviable' would result in a requirement to more than double the current threshold before addressing other factors.

The Future

3.32 The longer the levy exists as a subsidy/state-aided solution to the funding of racing, the more dependent on it racing will be.

3.33 The longer the levy exists as a subsidy/state-aided solution the less likely it is that a commercial alternative shall be introduced.

3.34 The levy is, by its very nature, a divisive mechanism. Every year bookmakers and racing, through the auspices of the HBLB, negotiate a new deal. Negotiations do not take the form of a commercial negotiation between a willing buyer and a willing seller but that of an adversarial environment that is damaging to what should be a positive relationship for mutual benefit.

3.35 The Committee believes that migration in the medium-term to a truly commercial relationship between bookmakers and racing is the only realistic option to achieve a long-term solution to the problems associated with the levy.

3.36 The levy should cease.

4 THE CAPACITY OF BOOKMAKERS TO PAY LEVY

Bookmakers' Total Contribution to Racing

4.1 It is wrong to assume that the levy, TV rights and sponsorship should be treated as separate; although one is a statutory payment, another, the result of a commercial relationship and the third a 'discretionary' spend, all come from the same source.

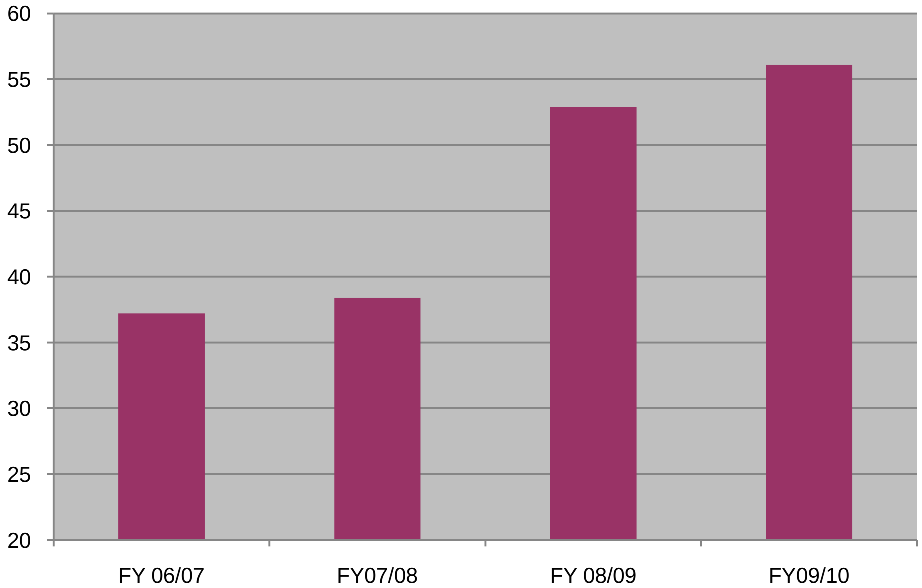
4.2 For the period 2006-9, racing received from bookmaking £565M excluding sponsorship.[14]

4.3 It has been argued previously that TV rights are not a commercial step towards the replacement of the levy but just another cost of doing business; and that the levy remains a statutory payment running in parallel to whatever commercial arrangements may from time to time exist.

4.4 The Committee believes this to be wrong when a majority of the cost of TV rights provides further direct funds to racing in addition to that which already exists through the levy. This was acknowledged by the Secretary of State in his comments on the determination of the 47th Levy Scheme.[15]

4.5 Although out-with the recommendations for the 50th Levy Scheme, the Committee believes that work towards migrating to a truly commercial relationship between bookmakers and racing should now commence. Work that when completed, should see a drawdown of the levy until its cessation.

Figure 4 Media Right Payments Received by Racecourses FY06/07 - FY09/10(£M).[16]



[14] Satellite Information Services Ltd.
[15] Paragraph 3.22
[16] Satellite Information Services Ltd.

4.6 **Figure 4** shows:

4.6.1 £38.4M received by racing (racecourses) for media rights in FY07/08.

4.6.2 £52.9M received by racing (racecourses) for media rights in FY08/09.

4.6.3 A 38% increase year-on-year from FY07/08 to FY08/09.

4.6.4 £56.1M received by racing (racecourses) for media rights in FY09/10.

4.7 Since 1st January 2008, a duopoly of TV supply has existed. Since that date a betting shop bookmaker requiring full coverage of British horseracing has had no choice but to buy content from both suppliers at whatever price each supplier charges.

4.8 This "must have" service for bookmakers wishing to remain competitive in the British horserace betting market, subject as it is to ever increasing contract fees, can not logically be viewed separately from levy payments and hides the true amount of money provided each year by bookmakers to racing.

4.9 The Turf TV initiative intended to raise greater revenue from the betting industry by selling to it the same content as previously, at a much higher price than had been paid hitherto, has reduced significantly bookmakers' overall profitability in respect of British horseracing.

4.10 This is not a sustainable position in circumstances where the cost of the commercial arrangements has increased significantly and is set to increase even further. Would, for example, racing still expect current levy sums to be unchanged if the sum received by racing for TV pictures was £100M?

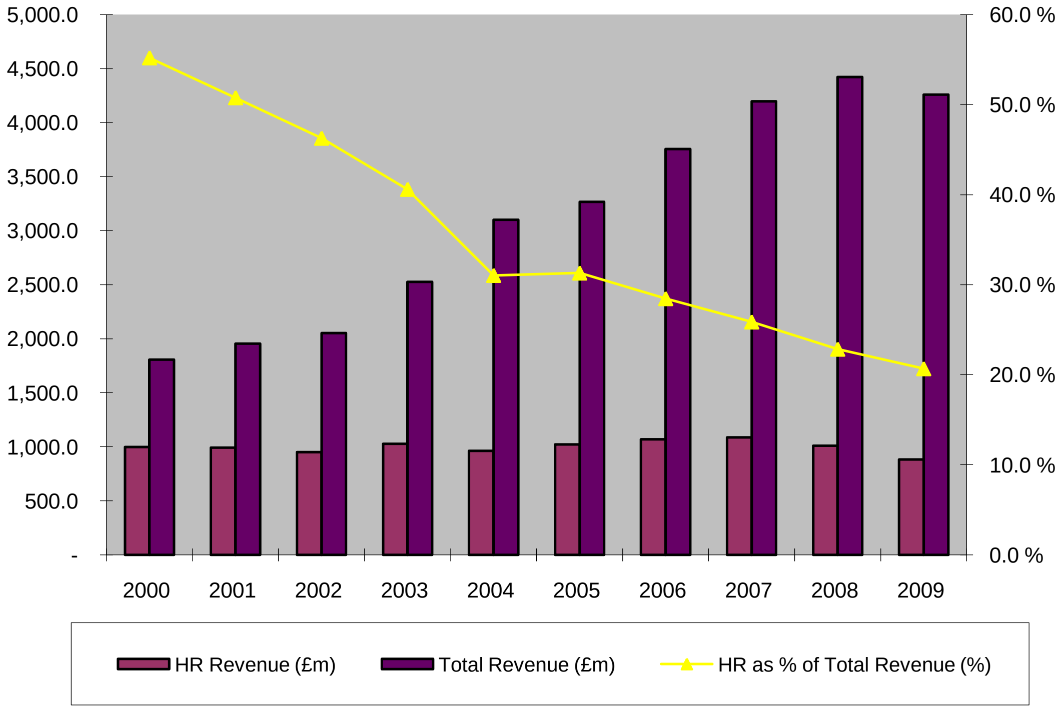
4.11 The betting industry should not be expected to accommodate a situation in which it is forced to pay more to racing under commercial arrangements whilst the levy in its present form remains in place.

The Reducing Market Share of British Horserace Betting Business

4.12 The importance of horseracing in total bookmakers' revenue has, since 2000, been constantly decreasing.

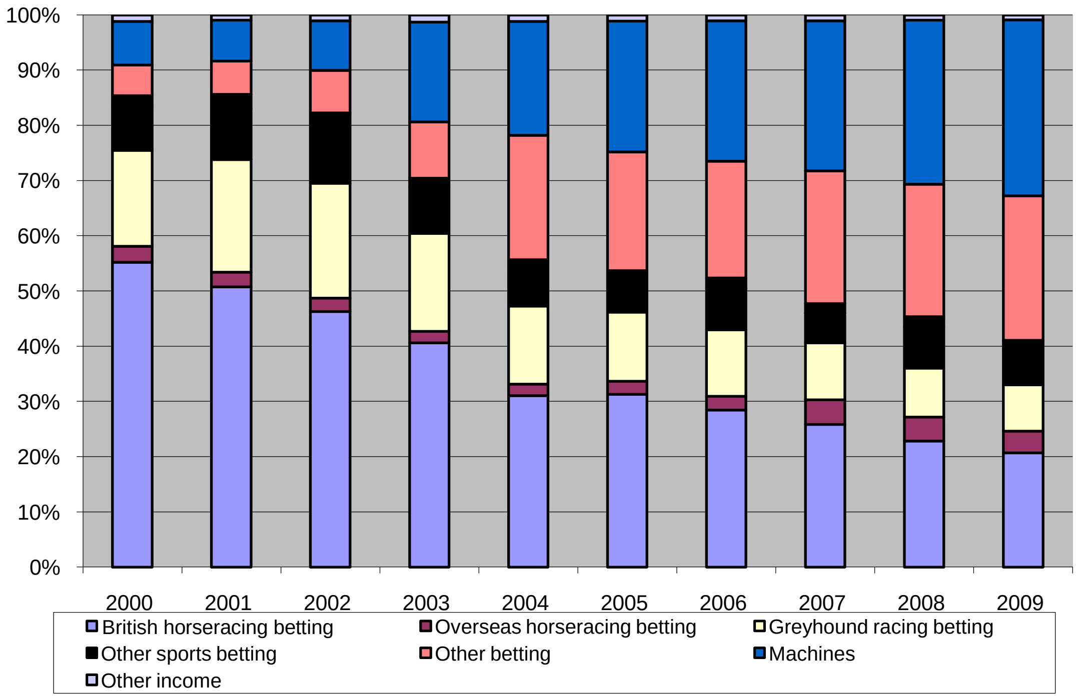
4.13 The British horserace betting share of bookmaker's revenue has dropped from 55.2% in 2000 to 20.7% in 2009. (**Figure 5)**

Figure 5 Share of British Horserace Betting in Bookmakers' Total Revenue.[17]



4.14 Trends in revenues from different betting products are illustrated in **Figure 6**. The market share in total gross win of particular betting products has changed significantly in recent years.

Figure 6 Gross Win from Betting Products.[18]



4.15 The market share of total gross win from British horserace betting has, with the exception of 2005, been in continuous decline since 2000.

[17] 50th Horserace Betting Levy Scheme 'Report for The Bookmakers' Committee', E&Y, 8th July 2010.
[18] Ibid.

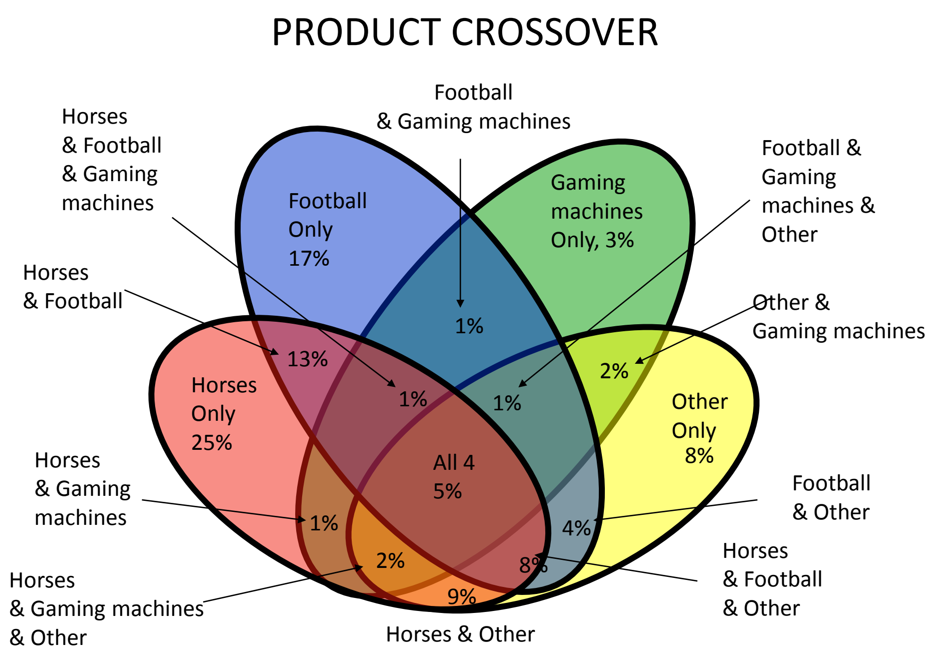
4.16 Football attracts 72% more Betfair ‘first bets’ than British horseracing.[19]

4.17 Such changes in gross win suggest that there is relative independence between different betting products, i.e., the introduction of machines and other betting products do not decrease betting on horseracing. This may be due to the fact that different groups of consumers have preference for different betting activities.

4.18 Although it is the case that approximately 43%[20] of LBO betting business is assumed to be British horseracing, this contribution has declined from 49% in 2003/04.

4.19 Information provided by one of the ‘Big 3’ bookmakers suggests that 64% of LBO customers are involved in some way with betting on British horseracing. However, only 25% are involved in betting on British horseracing exclusively. (**Figure 7)**

Figure 7 Product Crossover.



4.20 It is clear that substitution occurs two-way with other betting products and a “convoyed sales” argument could be used to reduce levy for the increased betting on British horseracing that is facilitated through the provision of wider betting services.

4.21 High costs (levy and media rights) will inevitably incentivise bookmakers to attempt to direct customers away from British horseracing towards more profitable products.

4.22 Racing continues to become more expensive to the bookmakers. It is quite possible that, if this were to continue, the current absolute reduction in horserace revenues could accelerate.

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[19] Betfair.
[20] Default percentage for the 48th Levy Scheme.

4.23 It is reasonable to assume that some gross win would transfer from racing to other products if racing were not available. Previous experience has suggested that this may be as much as 60%.[21] This gives a marginal value of British horseracing of only 40%. This is consistent with bookmakers' experience when racing has been disrupted for long periods due to weather or disease. If this is applied to work undertaken on behalf of the Bookmakers' Committee by London Economics[22] it can be seen at **Figure 8** that, excluding sponsorship;

Figure 8 Marginal Contribution of British Horseracing to the 'Big 3' Retail Estates.

Marginal Value of British Horseracing	**Ladbrokes 2009**	**William Hill 2009**	**Coral 2009**	**Aggregate 2009**
OTC Gross Win	427.4	459.1	316.5	1,203.0
B2/B3 Gross win	282.5	343.5	321.2	947.2
Total GB Retail Gross Win	709.9	802.6	628.5	2,141.0
Share Racing in OTC (default%)	43%	43%	43%	43%
Racing gross win	183.8	197.4	136.1	517.3
Marginal gross win from Racing @ 40%	73.5	79.0	54.4	206.9
-GPT	-11.0	-11.8	-8.2	-31.0
-Levy (8.8% average for 2009)	-16.2	-17.4	-12.0	-45.6
-TV Costs (est)	-17.8	-19.9	-13.3	-51.0
-Staff Costs (est)	-17.1	-16.3	-13.6	-47.0
Opportunity Costs	-15.0	-10.8	-8.2	-34.0
Total racing marginal costs	-77.1	-76.2	-55.3	-208.6
Racing Marginal Contribution (Profit/Loss)	-3.6	2.7	-0.8	-1.7
Racing Marginal Contribution (No levy)	12.6	20.1	11.2	43.9

40% Marginal Value Assumptions:

1. *If British horseracing were to cease, 60% of the existing British horseracing Gross Profit would be transferred to other betting products, hence the marginal value of British horseracing is only 40% of total British horseracing Gross Profit.*
2. *Racing gross win - represents 40% of British horseracing Gross Profit.*
3. *GPT - represents 15% of 'Racing gross win'.*
4. *Levy - 100% of the levy payment.*
5. *TV Costs(est) - 100% of British horseracing TV Costs (est).*
6. *Staff Costs (est) - assumes that staff costs do not fall as quickly as gross profit. (Uses 20% of British horseracing staff costs vice the 40% inferred by LECG analysis).*
7. *Opportunity Costs - 40% of the opportunity costs calculated by LE.*
8. *Total GB Retail Gross Win figures replicate LECG information presented previously. It is not used as all calculations are based on OTC gross win.*

[21] From Figure 7. 39% out of 64% who bet on British horseracing i.e. 39/64 = 61%.
[22] London Economics, 'An assessment of the Economic Arguments presented in Relation to the 50th Horserace Betting Levy'.

4.23.1 The marginal contribution of British horseracing to the ‘Big 3’ retail estates, before paying the levy, would be £43.9M.

4.23.2 The levy paid would be £45.6M.

4.23.3 This means that in those circumstances, the marginal loss suffered by the Big 3 retail estates, after payment of the levy, would be a loss of £1.7M.

4.23.4 TV costs represent a higher proportion of fixed costs in the independent sector and the marginal cost of British horseracing is therefore likely to be higher per shop. If this loss is representative of the retail betting industry as a whole then the marginal cost of British horseracing to LBOs is in the region of £2.5M per annum.

4.24 At current margins, the British horserace betting business is no longer attractive as an investment opportunity for commercial businesses. Unless this situation changes, particularly for the listed bookmakers, money will be allocated to other sectors which provide a greater return. Investment will reduce in proportion with increasing costs and reducing profits.

What Racing Costs Bookmakers

4.25 The cost of the levy is borne primarily by LBOs.

4.26 Increased and increasing TV costs are borne primarily by LBOs.

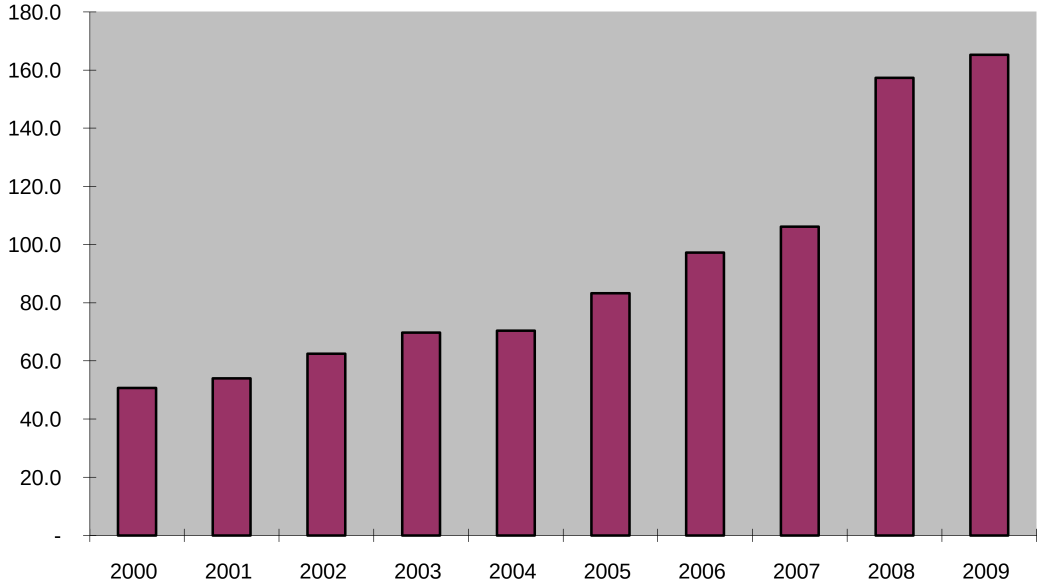
4.27 The levy as a share of British horserace gross win has been relatively constant for the last 10 years at an average of 9.0% (9.3% since 2002). It is lower than the headline rate of 10% set by the levy due to the fact that smaller shops pay an abated rate because of their reduced capacity to pay.

4.28 A bookmaker providing customers complete TV coverage incurs substantial costs in doing so. Although it is impossible to be definitive due to the commercial confidentiality of Turf TV and SIS contracts, cost per shop is approximately £23,000 inclusive of VAT. This will increase in January 2011.

4.29 The annual cost to the betting industry of providing TV coverage to LBOs is in the order of £200M.

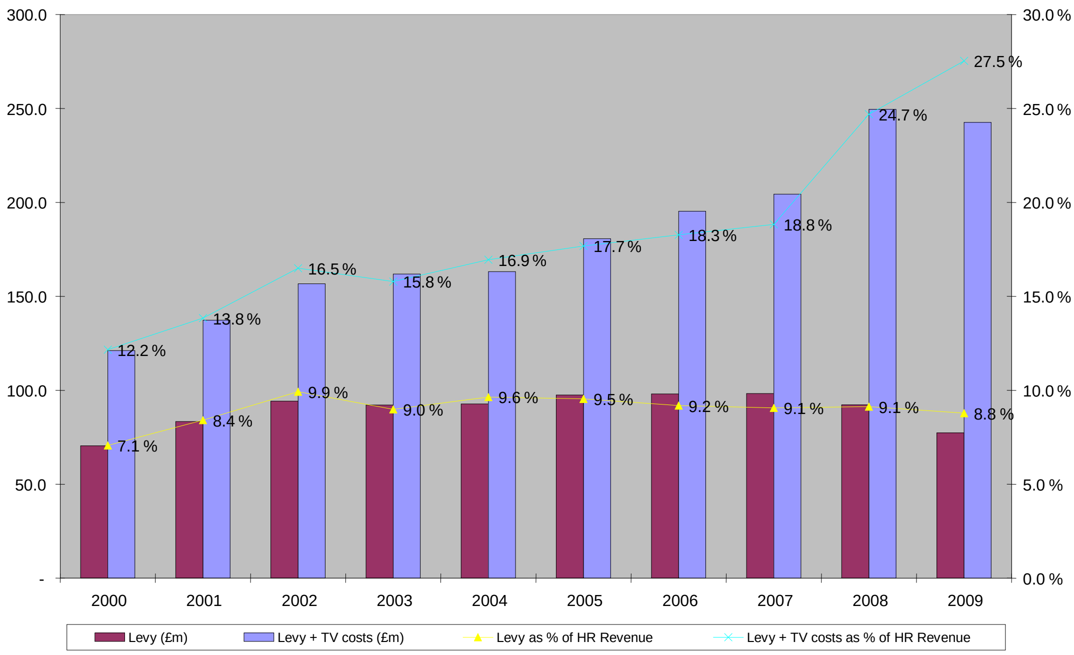
4.30 The cost of acquiring live horseracing pictures increased significantly from 1st January 2008, but were deemed too uncertain to take into account in the 47th determination. (**Figure 9)**

Figure 9 Changes in TV Costs(£M).[23]



4.31 Inclusion of TV rights costs leads to a considerably larger contribution by bookmakers to horseracing, particularly over the last 2 years. British bookmakers, and in particular retail LBO operators, now pay more in levy, TV costs and sponsorship, than ever before. The amount of bookmakers' horseracing revenue spent in this way has reached 27.5%. (**Figure 10)**

Figure 10 Levy as a Share of Bookmakers' British Horserace Betting Revenue.[24]



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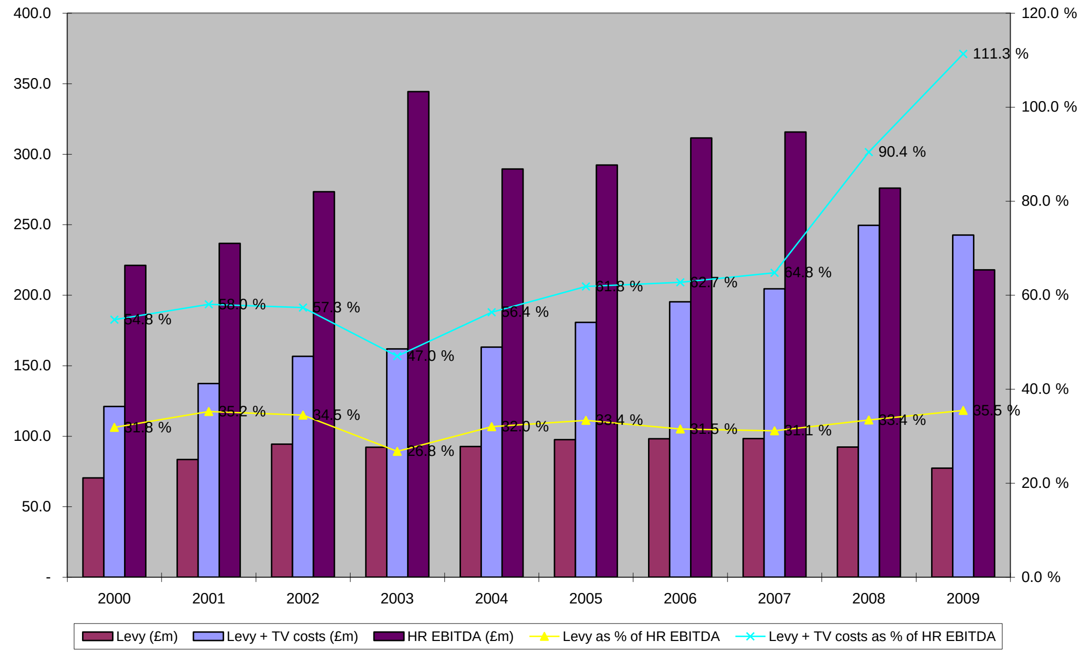
[23] 50th Horserace Betting Levy Scheme 'Report for The Bookmakers' Committee', E&Y, 8th July 2010.
[24] Ibid.

4.32 The indisputable fact is that bookmakers now transfer to racing, significantly more funds for the same content than they did prior to 1st January 2008, thus increasing their costs and reducing their overall profitability; particularly in respect of British horserace betting business.

4.33 The levy as a share of British horserace betting EBITDA has been relatively constant for the last years at an average of 32.3%. **Figure 11** shows that the inclusion of TV costs results in a considerably larger total cost to bookmakers, especially in the last 2 years. The cost of levy and total TV costs now exceeds bookmakers' EBITDA on British horseracing.

<u>Figure 11</u> Levy as a Share of Bookmakers' British Horserace Betting EBITDA.[25]

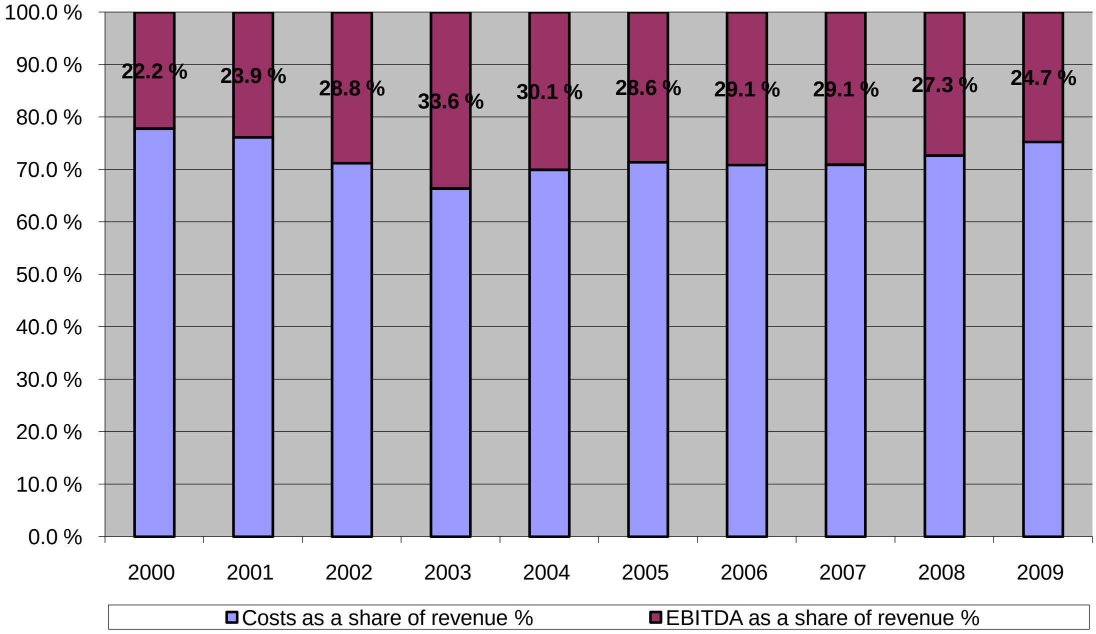


4.34 **Figure 12** assumes that all betting products have the same EBITDA margins ie: it allocates costs in-line with margins. This is likely to overstate horserace betting EBITDA as some costs, such as media rights, should be wholly allocated to this segment.

4.35 The profitability of British horseracing has decreased due to decreasing revenues from horserace betting and increasing costs. Lower EBITDA from horserace betting decreases bookmakers' capacity to pay.

[25] Ibid.

Figure 12 Horserace EBITDA and Costs.[26]

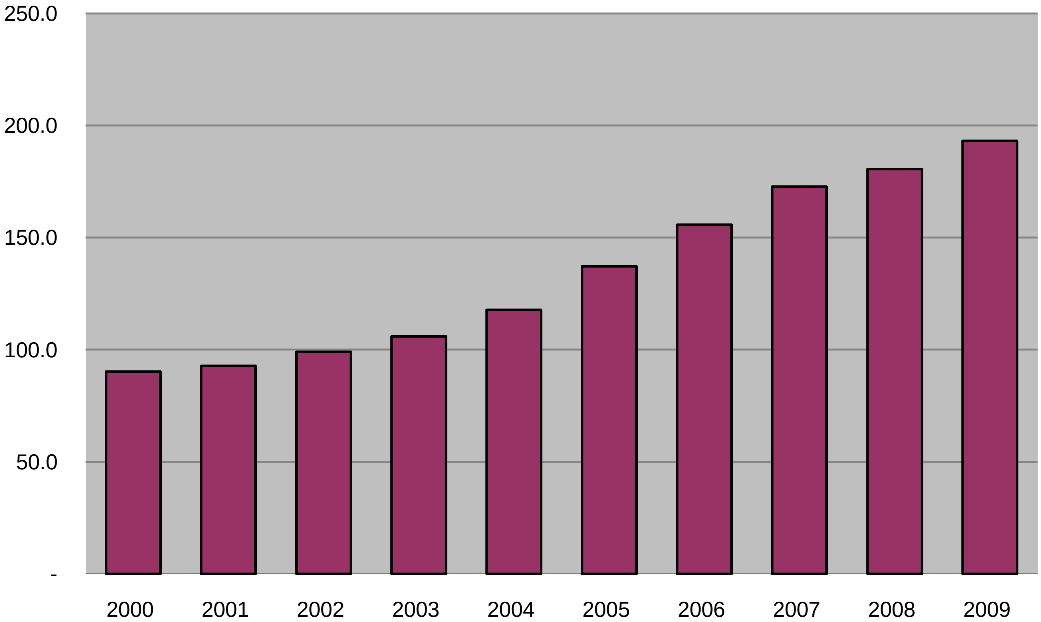


4.36 Costs having an indirect impact on British horseracing include

4.36.1 Gambling Commission fees and compliance costs, which are now substantial and increasing above inflation. These costs were minimal prior to the Gambling Act coming into effect in September 2007.

4.36.2 increases in rent and rates at above inflation rates. (**Figure 13)**

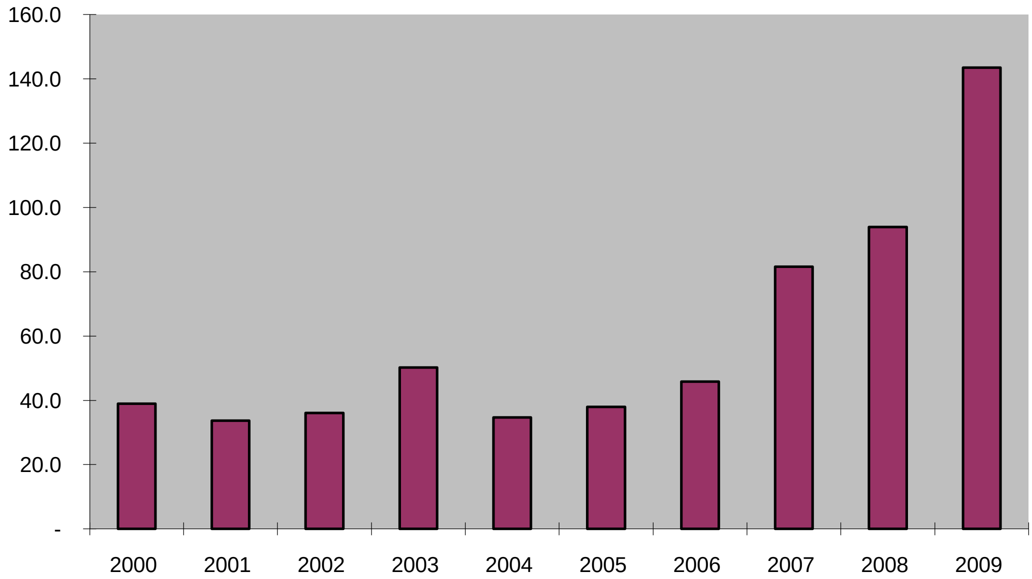
Figure 13 Changes in Rent and Rates Costs(£M).[27]



[26] Ibid.
[27] Ibid.

4.36.3 Increased marketing costs. This is no longer a discretionary spend given the competitive markets in the UK and abroad. Such an environment requires companies to spend just to maintain their existing position. (**Figure 14)**

Figure 14 Changes in Marketing Costs(£M).[28]



4.37 Overall, bookmakers' costs have increased and continue to do so; most are rising faster than inflation, leading to diminishing profitability and consequently, the ability of the bookmaker, and in particular bookmakers running betting shops, to pay the levy.

4.38 We anticipate little or no growth against which to off-set such costs.

4.39 The industry's capacity to pay the levy is inevitably reduced.

The Economy

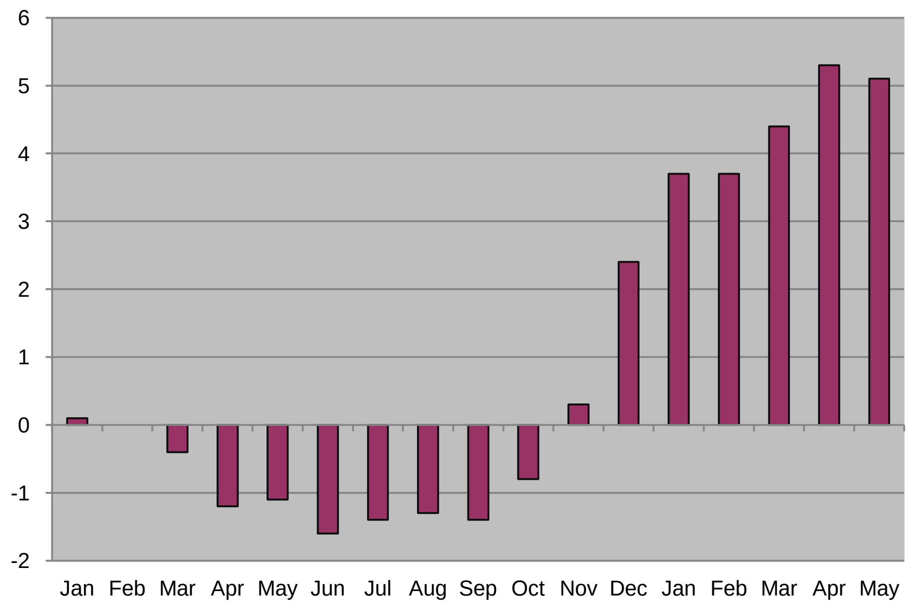
4.40 The economic outlook for the UK is not good. This will affect both bookmakers and racing. The Office for Budget Responsibility highlights that GDP for Q1 2010 was 0.3%. This is 0.2% less than Q1 2009.

4.41 Costs are rising.

4.42 Office for National Statistics figures show Retail Prices Index inflation rose from -1.1% in May 2009 to 5.1% in May 2010. **(Figure 15)**

[28] Ibid.

Figure 15 Retail Price Index Jan 2009 – May 2010(%).[29]



4.43 The 50th Levy Scheme will commence on 1st April 2011 by when many of the decisions announced in the budget of 22nd June 2010 shall have come into force. Several will have the effect of reducing the level of disposable income available to punters.

4.44 GDP growth for 2011 is now estimated at 2.6%. It is generally acknowledged that 3% is required to keep employment in equilibrium.

4.45 UK interest rates have remained at 0.5% for 16 months. The Organisation for Economic Co-operation & Development (OECD) believes UK interest rates could rise to 3.5% by the end of 2011, limiting further, punters' spend and capacity of bookmakers to pay levy.[30]

4.46 Office for National Statistics figures show that the Consumer Price Index (CPI) for May 2010 was 3.4%.

4.47 Office for National Statistics figures show the level household expenditure for CY 2010 Q1 was 0.5% lower than CY 2009 Q1.

4.48 The bookmaking industry within the UK is a significant employer. It has to date remained so during the economic downturn and should wish to continue in the future, despite the bleak economic outlook. Bookmaking has 'cut its cloth'.

4.49 Significantly increased costs shall undoubtedly lead to shop closures and job losses across an industry that employs circa 40,000 people. These impacts fall out-with the levy per se, but must be taken into account as a direct consequence of decisions taken prior to 1st April 2011.

4.50 Currently, no estate growth is allowed, minimal economic growth is forecast and as such a further increase in payments to racing can not be justified.

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[29] Office for National Statistics
[30] www.oecd.org

4.51 It appears irrational to the Bookmakers’ Committee to grow the subsidy from one internationally competitive industry to another, at a time of public spending cuts across all areas, which runs counter to current economic policy and thinking in both the UK and the EU. This is particularly stark given the increased income to racing from other sources.

5 ATTENDANT ISSUES

5.1 The Committee believes that an increase in levy could result by addressing the following:

Non-runners

5.2 The betting industry has been making representation against 48-hour Declarations since the end of 2006. To restate the obvious, the changeable climate in the UK means that there are frequently significant going changes in the 48-hour period between the time of declaration and the time of the race. This inevitably leads to a higher level of non-runners than under the 24-hour Declaration system which applies to National Hunt racing.

5.3 There is evidence to show that there are more non-runners resulting from 48-hour Declarations for turf flat racing than for National Hunt racing, despite all the vagaries of the latter.

5.4 The trainer self-certification policy continues to detract from the customer's confidence that a particular horse will actually run.

5.5 Field size limits continue to have an effect on the maximum number of runners which can be declared for individual races. In these circumstances, non-runners further reduce actual field sizes, which impacts off-course betting levels on, for example, each-way betting.

5.6 Non-runners put punters off; they like to know where they stand when placing bets and a multiple which collapses because one or more of the original selections does not run is a major disincentive. Multiples, of course, are high margin bets so the negative effect on profits and levy is disproportionately great.

5.7 We recognise that the incremental income, consequent upon 48-hour declarations forecast by the broadcasters including, ultimately, co-mingling fees, may outweigh the loss to the levy caused by lower profits from leviable fixed-odds betting. However, it remains clear that the choice for racing lies between these two sources of income; it seems unlikely that both can deliver in parallel.

Fixture Planning

5.8 We consider that the BHA fixture review completed in May 2008 tried to satisfy too many of racing's constituents. Whilst we understand the overall finding that ever more racing was spreading resources (e.g. horse population, racing's regulatory infrastructure, stable staff, etc) too thinly, the changes put in place to address the issue were surprisingly illogical.

5.9 We feel it is appropriate to revisit the concept suggested by the Committee previously of a reduction in the number of fixtures whilst maintaining the total number of races.

5.10 The Committee notes the BHA intention to remove its circa 250 fixtures from the racing calendar. We consider this will have potentially significant impact and in noting racing's desire to reduce the number of fixtures, consider it, along with other attendant issues, very likely to weaken the ability of the bookmaking industry even further, to generate levy.

5.11 The Committee intends to continue to support the fixture planning efforts of the HBLB and BHA through the Betting Patterns Working Party.

Distribution of Pictures into LBOs

5.12 The Board is already aware that the uncoordinated distribution of pictures to betting shops offers a very poor experience for customers. New products are being offered by different distributors which serve as an alternative to British horseracing thus diluting its content. This has, predictably, led to a much inferior overall presentation of British horseracing. There is some evidence that, on a like-for-like basis, the gap in the rate of decline between horseracing and general over-the-counter transactions is increasing and continues to do so.

Provision of Live British Horseracing TV Pictures direct to Homes

5.13 The availability of home TV coverage has diluted the 'pull' of LBOs and consequently their ability to increase footfall in relation to British horseracing. The Committee understands fully the commercial imperative behind racing's decision in this respect in an attempt increase funding; however, this has significantly weakened the ability of the LBOs to generate increased levy income.

5.14 Customers choosing to watch the racing at home are increasingly likely to bet with bookmakers not paying levy.

Availability of Live Pictures via Internet Streaming

5.15 For little or no cost (such as a small bet), a customer can watch all British horseracing live via internet streaming. This also is diverting business from levy generating LBOs to bookmakers outside the scope of the levy.

6 THRESHOLDS AND INCENTIVISATION

6.1 The Committee co-operated with the HBLB in its review of thresholds and incentivisation.

6.2 The Committee has little doubt that the requirement of the Act that there should be 'categories', requires the Committee to make relief for small bookmakers. Every levy scheme to date has made such provision, often, as in the 2002 Determination, at a far higher level than the current Scheme.

6.3 A principal advantage of the threshold system is that it incentivises racing to become more attractive to punters, because the marginal rate of levy is in excess of the headline rate. This is because increasing a shop's gross profit from horseracing will increase the rate payable.

6.4 In the OCP report dated 21st January 2008, commissioned by the Minister to assist him in the determination of the 47th Scheme, there was clear recognition of the importance of the threshold system:

'*We therefore suggest that the threshold be indexed for inflation and, if a lower levy yield is adopted, consideration be given to increasing the threshold by an appropriate amount as opposed to each basis point reduction in the rate.'*

It also stated

'Restoration of the real 2002-3 value of the threshold would be consistent with the 2002-3 determination. It would take into account the capacity to pay of each bookmaker considered separately. It would almost certainly prevent the closure of a number of small shops, probably preserving betting shop facilities in some areas where they would otherwise cease.'

6.5 The threshold for the 41st Levy Scheme was set by the Minister at £150,000. That rate would now be £190,118.[31]

6.6 The Committee gave serious and lengthy consideration to the options open to it and believes that the only equitable way to keep shops open is to increase the threshold. Those shops are now contributing to racing, if more close, the burden of supporting British horseracing will fall on the remaining shops, which will make even more shops uneconomic.

6.7 In recognition of the difficulties faced by this sector, as set out previously, the Committee consider that an increase in threshold is justified.

[31] Source: Ernst & Young (as at May 2010)

7 RECOMMENDATIONS FOR THE 50TH LEVY SCHEME

7.1 The Committee recommends that the levy should continue to be based on a percentage payment of bookmakers' gross profits on horseracing business conducted in Great Britain. For the purposes of the 50th Levy Scheme, this term shall mean the gross profit derived from horserace betting business conducted on horseracing taking place in England, Scotland and Wales only.

7.2 Rates: LBO/Telephone/Internet Bookmakers. Bookmakers making gross profit via betting on British horseracing on these channels should continue to pay 10% of gross profit as levy.

7.2.1 LBO Threshold. As in previous years, an increase in the threshold figure at which the headline rate of levy is payable by the LBO sector is recommended. The recommendation is that reduced charges should apply for all shops showing a relevant gross profit of less than £123,000. Shops with a gross profit of less than £123,000 will pay a rebated charge on a sliding scale related to the percentage by which their gross profit falls short of £123,000.

7.3 Rates: Bookmakers Engaged in Spread Betting. We recommend that bookmakers who derive their gross profit from spread betting businesses should pay levy at 2% of such gross profit, where it arises from British horseracing.

7.4 Rates: Betting Exchanges. We recommend that betting exchanges should continue to be assessed for levy on the basis of 10% of their gross profit on British horseracing business, where gross profit is defined as the commission deducted by the exchange from the amounts paid out by it to bettors and bet-takers.

7.5 Racecourse Bookmakers. We recommend that the previous annual fixed fee for racecourse bookmakers who stand at licensed racecourses should be retained, with the proposal that the fee should be set at £210[32] per annum.

7.6 Point-to-Point Only Bookmakers. In respect of bookmakers who stand only at point-to point events and/or at harness-racing and/or trotting events, the Committee would propose that their annual fixed contribution should be increased in line with RPI to £166[33]. Bookmakers who otherwise pay levy under other clauses would be exempt from any additional payment under this sub-paragraph.

7.7 Default Percentage. The Committee recommends that bookmakers who are unable to measure their British horseracing gross profit be required to base their declarations for levy on the average percentage of gross profit attributable to British horseracing achieved by Ladbrokes plc, Gala-Coral Group, William Hill plc and Corbetts in their combined LBO estates during the calendar year 1st January – 31st December 2011. We will seek to expand the number of independents in the sample.

[32] Based on assumed RPI of 5% on 31st Jul 10.
[33] Based on assumed RPI of 5% on 31st Jul 10.

ANNEX A

DERIVATION OF RECOMMENDED THRESHOLD USING THE 48TH LEVY SCHEME

		50th Levy Scheme				48th Levy Scheme			
		Total Shops		Threshold =	123,000	**Total Shops**		Threshold =	90,000
				Rate =	10.00%			Rate =	10.00%
Shop Banding - £	Average Gross Profit *	Nos.	Gross Profit £'000	Levy £'000	%	Nos.	Gross Profit £'000	Levy £'000	%
0-4999	602	73	43,923	£21	0.05%	73	£43,923	£145	0.33%
5000-9999	7759	41	318,139	£2,007	0.63%	41	£318,139	£2,821	0.89%
10000-14999	12821	61	782,063	£8,152	1.04%	61	£782,063	£11,238	1.44%
15000-19999	17772	104	1,848,245	£26,704	1.44%	104	£1,848,245	£36,640	1.98%
20000-24999	22676	152	3,446,694	£63,541	1.84%	152	£3,446,694	£87,031	2.53%
25000-29999	27614	218	6,019,793	£135,145	2.25%	218	£6,019,793	£184,852	3.07%
30000-34999	32753	305	9,989,559	£266,004	2.66%	305	£9,989,559	£363,724	3.64%
35000-39999	37597	369	13,873,289	£424,060	3.06%	369	£13,873,289	£579,683	4.18%
40000-44999	42456	386	16,388,014	£565,666	3.45%	386	£16,388,014	£773,253	4.72%
45000-49999	47486	457	21,700,991	£837,795	3.86%	457	£21,700,991	£1,144,926	5.28%
50000-54999	52511	471	24,732,511	£1,055,870	4.27%	471	£24,732,511	£1,442,935	5.83%
55000-59999	57545	471	27,103,628	£1,268,028	4.68%	471	£27,103,628	£1,732,703	6.39%
60000-64999	62426	474	29,589,731	£1,501,753	5.08%	474	£29,589,731	£2,051,985	6.93%
65000-69999	67542	486	32,825,250	£1,802,498	5.49%	486	£32,825,250	£2,462,928	7.50%
70000-74999	72337	461	33,347,467	£1,961,190	5.88%	461	£33,347,467	£2,679,696	8.04%
75000-79999	77508	431	33,405,922	£2,105,060	6.30%	431	£33,405,922	£2,876,206	8.61%
80000-84999	82553	390	32,195,632	£2,160,848	6.71%	390	£32,195,632	£2,952,489	9.17%
85000-89999	87486	343	30,007,542	£2,134,330	7.11%	343	£30,007,542	£2,916,185	9.72%
90000-94999	92459	359	33,192,864	£2,495,111	7.52%	359	£33,192,864	£3,319,286	10.00%
95000-99999	97489	290	28,271,704	£2,240,788	7.93%	290	£28,271,704	£2,827,170	10.00%
100000-104999	102530	270	27,683,123	£2,307,604	8.34%	270	£27,683,123	£2,768,312	10.00%
105000-109999	107342	220	23,615,230	£2,060,898	8.73%	220	£23,615,230	£2,361,523	10.00%
110000-114999	112474	212	23,844,587	£2,180,412	9.14%	212	£23,844,587	£2,384,459	10.00%
115000-119999	117443	164	19,260,676	£1,839,052	9.55%	164	£19,260,676	£1,926,068	10.00%
120000-124999	122502	132	16,170,269	£1,610,480	9.96%	132	£16,170,269	£1,617,027	10.00%
125000-129999	127243	131	16,668,806	£1,666,881	10.00%	131	£16,668,806	£1,666,881	10.00%
130000-134999	132509	141	18,683,740	£1,868,374	10.00%	141	£18,683,740	£1,868,374	10.00%
135000-139999	137529	85	11,689,956	£1,168,996	10.00%	85	£11,689,956	£1,168,996	10.00%
140000-144999	142419	77	10,966,269	£1,096,627	10.00%	77	£10,966,269	£1,096,627	10.00%
145000-149999	147330	67	9,871,107	£987,111	10.00%	67	£9,871,107	£987,111	10.00%
150000-154999	152301	55	8,376,556	£837,656	10.00%	55	£8,376,556	£837,656	10.00%
155000-159999	157046	41	6,438,901	£643,890	10.00%	41	£6,438,901	£643,890	10.00%
160000-164999	162480	29	4,711,913	£471,191	10.00%	29	£4,711,913	£471,191	10.00%
165000-169999	167355	40	6,694,197	£669,420	10.00%	40	£6,694,197	£669,420	10.00%
170000-174999	172444	18	3,103,988	£310,399	10.00%	18	£3,103,988	£310,399	10.00%
175000-179999	177355	17	3,015,036	£301,504	10.00%	17	£3,015,036	£301,504	10.00%
180000-184999	182929	15	2,743,935	£274,394	10.00%	15	£2,743,935	£274,394	10.00%
185000-189999	187110	21	3,929,317	£392,932	10.00%	21	£3,929,317	£392,932	10.00%
190000-194999	192224	10	1,922,238	£192,224	10.00%	10	£1,922,238	£192,224	10.00%
195000-200000	197428	10	1,974,276	£197,428	10.00%	10	£1,974,276	£197,428	10.00%
>200000	285538	51	14,562,446	£1,456,245	10.00%	51	£14,562,446	£1,456,245	10.00%
LEVY INCOME - SHOPS			615,009,527	43,588,289	7.09%		615,009,527	52,038,554	8.46%
* Average Gross Profit is the average within that band for the 48th Scheme.									