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No. ACT of 2017

Tabcorp Holdings Limited

Proposed acquisition of Tatts Group Limited by Tabcorp Holdings Limited way of scheme of arrangement

STATEMENT OF RAY GUNSTON

Statement of:	Ray Gunston
Address:	806/1 Queensbridge Square, Southbank Victoria
Occupation:	General Manager of Finance, Corporate and Major Projects at the Australian Football League
Date:	24 February 2017

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I, Ray Gunston, General Manager of Finance, Corporate and Major Projects at the Australian Football League, say that:

BACKGROUND

1. I am the General Manager of Finance, Corporate and Major Projects at the Australian Football League (**AFL**).
2. I am also a non-executive director of Sigma Pharmaceuticals Limited and Hotel Property Investments Limited.
3. Between 2000 and 2012, I was the Chief Financial Officer of Tatts Group Limited.
4. I have also acted as a consultant to the racing industry and various government bodies, including the Western Australian Racing Representative Group (**WARRG**), where I published a report in 2014 commenting on the potential privatisation of the Western Australian TAB (known as the 'Gunston Report'). A copy of this report is attached at **Annexure RG-1**.
5. I was also a director of the Essendon Football Club during 2007, as well as the club's interim CEO between 2013-2014, and a non-executive director of AFL Victoria between 2009-2011.

Personal involvement in the wagering industry

6. As CFO of Tatts for approximately 12.5 years, I had significant involvement in a major participant in the Australian wagering industry and had knowledge and awareness of Tatts' ongoing relationship with the racing industry.
7. I have also acted as a consultant to WARRG which resulted in the publication of the Gunston Report in 2014. The process of preparing this report required me to have an intimate and detailed working knowledge of the wagering industry in Australia and the key players and stakeholders that would be affected by privatisation if it were to occur. I was required to be in a position to make a number of recommendations for the WA Racing Industry as to the future structure of the Western Australian wagering industry, and whether the West Australian TAB (**WATAB**) privatisation would continue to deliver funding flow throughs to the racing industry.
8. As such, I consider that I have a detailed knowledge and understanding of the wagering industry in Australia, and its relationship with the racing industry.

OVERVIEW OF THE GUNSTON REPORT

9. In 2014, I was commissioned by WARRG to assist the Group in preparing a report on the viability and pathways to the privatisation of the WATAB.
10. The aim of the report was to:

    a. explain the concept of privatisation, having reference to the privatisation processes that have taken place in other Australian states and territories;

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b. establish a base-line position of the Western Australian racing industry for communication to industry participants and the Government covering areas such as financial flows from privatisation;

c. outline and assess the potential implications of privatisation from an industry structure and finance perspective; and

d. discuss different privatisation structures.

11. Currently, WATAB sits within the operations of Racing and Wagering Western Australia (**RWWA**). Privatisation of the wagering operation would therefore require a process of separating out WATAB from within RWWA, and then seeking the sale of WATAB to a private entity or a publicly listed company. Similarly to TABs in most other states and territories in Australia, the wagering operations of WATAB provide funding for the Western Australian racing industry (i.e. the local industry).

12. In terms of wagering performance, WATAB for the 6 year period to 2013 had a high turnover growth relative to TAB operations in other states and territories, which in my view primarily reflected catching up in revenues to these other TABs who had previously implemented the product and technology initiatives underpinning this out-performance. However, WATAB has faced considerable competition from corporate bookmakers, and this continues to be the case. Thus, the Gunston Report emphasised that the benefits of, and need for, scale and ongoing investment within a larger TAB wagering operation should be considered in light of the consolidation of TABs throughout Australia into either the Tabcorp or Tatts group.

13. The need for increased scale and larger wagering operations and pools led to RWWA outsourcing the management of its wagering services to two operators: pari-mutuel wagering is pooled into Tabcorp's SuperTAB pool, while fixed odds betting is managed by William Hill, a corporate bookmaker based in the Northern Territory. These pooling arrangements arguably present a long term risk to WATAB/RWWA as they are dependent on third parties for the supply of critical services, third parties that are effectively competitors in the wagering market.

14. The Gunston Report offered no opinion on whether privatisation was in the best interests of WATAB. However, I made a number of key observations/ recommendations, including:

a. the privatisation of WATAB is a complex task, involving a range of stakeholders, the primary stakeholder being the WA racing industry;

b. any privatisation in the future must adopt a model that ensures the racing industry is 'no worse off' in terms of a funding model. The WA racing industry cannot support privatisation unless such a funding model is guaranteed;

c. if a long term exclusive retail totalisator licence is offered for the privatised entity for both pari-mutuel and fixed odds betting, with an obligation to meet WA racing industry funding, shorter term review points should be inserted in the wagering licence to test the appropriateness of the racing industry funding model and the operation of the licence;

d. the WA racing industry must pursue alternatives for infrastructure funding irrespective of whether privatisation occurs, given the WA racing industry currently has little or no capacity to fund infrastructure maintenance and development; and

e. racefield fees currently flow to RWWA, not specifically to WATAB, and hence the current structure would need to be re-examined if privatisation were to occur.

OVERVIEW OF THE WAGERING INDUSTRY

15. The Australian racing industry is made up of three codes - thoroughbred, harness and greyhound racing.
16. The major participants in the racing industry are:
    a. the punters – people who place the bets on racing, sports and other events with wagering operators;
    b. the wagering operators – organisations that provide the parimutuel and fixed odds wagering products;
    c. the racing industry – the racing clubs and associations, administrators, breeders, owners, trainers, jockeys/drivers and their employees;
    d. media broadcasters – the companies who provide the vision of the races through various arrangements; and
    e. the State or Territory Government – which establishes the regulatory, integrity and licensing frameworks for the conduct of racing and wagering.
17. The wagering operators that provide betting services within Australia can be classified into the following groups:
    a. on-course bookmakers – those who are licensed to provide fixed odds betting in each state and territory at racing venues;
    b. corporate bookmakers and/or betting exchanges – licensed off-course bookmakers who typically operate via telephone and internet/mobile applications (see paras 26 to 29 below);
    c. TABs – Totalisator Agency Boards (**TABs**); and
    d. offshore bookmakers operating illegally into Australia.
18. There are two main types of wagering. Totalisator or pari-mutuel betting is a betting system in which all bets of a particular type on specific events are placed together into a single pool. A set percentage of that pool is paid back in winning bets, and the rest is retained by the TAB as a commission to pay taxes, meet its costs, and pay other requirements such as funding to the

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racing industry. As the pool grows from the bets being placed, the amount available to be paid for winning bets grows. With totalisator betting (as distinct from fixed odds betting) the possible dividends keep moving until the time for betting closes. Currently, parimutuel betting can only be provided by TABs in Australia. However, a number of corporate bookmakers re-sell tote dividends through tote derivative products. The tote derivative products essentially replicate tote odds, by offering punters the highest tote payout available across the UBET, SuperTAB and NSWTAB pools.

19. Fixed odds betting is a form of wagering where the punter receives and retains the odds that have been quoted to them at the time they place the bet. In this type of betting, the wagering operator is not assured of a profit, with profitable outcomes for the wagering operator dependent upon their skills at managing the risk of the range of probabilities for different outcomes. This form of betting is therefore riskier for the wagering operator than totalisator betting, as a profit margin is not guaranteed.

20. Totalisator Agency Boards were established in each state or territory between 1961 and 1985 to provide a legal vehicle for race wagering and to facilitate the racing industry receiving funding. The intention was to remove all betting predominately with illegal 'SP [starting price] bookmakers', who were not paying the racing industry for its product, being the putting on of races at race tracks. TABs were set up by government legislation and were given authority/licence to exclusively operate pari-mutuel betting for off-course retail, and for on-course in certain jurisdictions. In exchange for this exclusivity, TABs had an obligation to fund the local racing industry. TABs have since expanded their product offering to include fixed odds products (although these are non-exclusive except at retail) and now also provide both on-line and telephone wagering services.

21. TABs in all states are now privatised, with the exception of WATAB. There has also been significant consolidation within the TABs in terms of ownership/licence holding arrangements over the course of the last two decades. As of today, there are three TAB owners operating throughout Australia:

    a. Tabcorp Holdings Limited (**Tabcorp**);

    b. Tatts Group Limited (**Tatts**); and

    c. WATAB/RWWA.

22. As a result of the way the wagering industry has been structured, the racing industry has therefore historically been heavily reliant on the tote for funding.

23. Given these features, a tote operation relative to corporate bookmakers will generally provide more certainty in terms of funding for the racing industry. The way the tote works means there

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is greater certainty that a fixed proportionate amount will be channelled back through to the racing industry for every bet placed. This model therefore ensures industry funding is not dependent on the wagering result. In contrast, funding based on gross revenue or turnover of fixed odds betting could mean that there is variability in how much will be flowed through to the racing industry, or in capacity to pay. Therefore, provided there is sufficient turnover in the pari-mutuel pools, there is no capital risk associated with the pari-mutuel funding model and it provides a stable basis for racing industry funding. In addition, the lack of risk in supplying pari-mutuel wagering services means that there will generally be less need for any restriction on the way a punter bets into the pool.

24. It is my view that pari-mutuel betting has a distinct and valuable role for the wagering industry for a number of other reasons, including:

    a. the pari-mutuel pool provides a stable liquidity base to the wagering industry, with the volume of pools providing punters and corporate book makers with a basis of risk management for offsetting unacceptable risk exposures; and

    b. an increased skill based wagering proposition for punters of choosing if and when to seek to obtain, in their view, the best odds through fixed odds betting or leaving it to the final pari-mutuel dividend outcome.

25. The tote model and engagement with the racing industry are also directly related and indeed co-dependent. Funding from the wagering industry contributes significantly to the amount of prize money offered on races, and this point was reinforced from my experience with the West Australian industry. Sufficient prize money is essential to keeping owners and trainers investing in quality horses / greyhounds, and engaging in the industry in general. Where prize money amounts are not growing or are insufficient, owners will tend to reduce their investment in horses/greyhounds and/or send them interstate or even overseas to better funding models. A decline in the quality of the race field results in a corresponding decline in punter engagement with the racing industry, which has an immediate and direct effect on the wagering industry.

RISE OF CORPORATE BOOKMAKERS

26. I am aware of the rise in the number of corporate bookmakers in the Australian wagering market over the past 20- 25 years. These businesses are principally licensed in the Northern Territory due to the lower wagering duties and taxes, and lower licensing fees compared to other states and territories.

27. In many cases, the objective of these businesses initially was to grow market share based on wagering turnover, and to create a large customer base, through aggressive pricing and marketing, without profitability necessarily being a priority. This model was adopted to enable

the corporate bookmakers to establish businesses of sufficient scale and customer penetration that could be attractive for potential large corporate bookmakers prepared to pay premiums for market access. This has played out in recent times.

28. The rapid growth of corporate bookmakers can also be attributed to the fact that TABs had not developed quickly enough with their fixed odds offerings and technology-based wagering platforms. The corporate bookmakers took advantage of their low costs licences to provide more attractive odds through their fixed odds and tote derivative products.

29. It is my view that there are significant imbalances between the totes and corporate bookmakers in terms of funding to the racing industry in that corporate bookmaker contribution rates continue to remain at low levels relative to their market share and position in Australia. While the economic model for corporate bookmakers was impacted slightly by the introduction of racefield fees through state government legislation in 2008 and 2009, this measure has failed to stimulate sufficient funding to the racing industry from corporate bookmakers. As a consequence, the racing industry continues to rely heavily on the tote for its funding.

VIEWS ON THE VICTORIAN AND WESTERN AUSTRALIAN WAGERING LICENCES

Western Australia

30. While WATAB/ RWWA is responsible for off-course wagering via retail outlets, I consider this to be an asset facing significant value diminution risk. The financial position of RWWA has meant that ongoing capital investment required to continue to improve the retail offering of WATAB is limited. As such, I am of the view the that this negatively impacts on the value of the Western Australian wagering licence. This of course depends upon how such a licence and sale price is structured, particularly the levels of required racing industry funding and any taxation arrangements.

31. If the privatisation process occurs, I consider that Tabcorp, and most likely Tatts, would be interested in bidding for the asset. I also consider that there is a possibility that other wagering operators, such as potentially certain corporate bookmakers, could also consider purchasing the asset. The value that any party places on the licence will depend on their strategic objectives, their attitude to the views I express above, and to the extent to which they can extract synergies between the WATAB business and their own other operations.

32. Tabcorp and Tatts would be expected to be able to extract substantial synergies from an investment in WATAB as a result of their existing TAB wagering operations in other Australian states and territories.

33. It is possible that other wagering operators would see some potential synergies or have some strategic value in acquiring the WATAB business. For example, CrownBet has an existing

presence in WA through its ownership of Perth Casino and it operates Keno and owns the rights to the Trackside product in WA. However, its recent initiative with Clubs NSW may suggest it would look at alternate models to a TAB. Other corporate bookmakers operating in Australia such as Ladbrokes have existing experience in running retail wagering networks in the UK and may see some complementarity.

34. Likewise, it is conceivable that the Hong Kong Jockey Club or Singapore Turf Club – which both run large pari-mutuel pools – could see Western Australia as an opportunity to enter the Australian retail wagering market.

35. However, I am of the opinion that due to the challenges faced by the WATAB business, the Western Australian government might not solely rely on a competitive process to maximise industry funding and the proceeds that it receives from a bid. In conducting a privatisation, the Western Australian government could be in a position to ensure that appropriate funding frameworks are in place, and to structure any bidding or negotiation process in a way that allows it to achieve a good outcome through other sale approaches.

Victoria

36. I am aware that the Victorian licence for wagering and betting is due to expire in 2024.

37. The Victorian retail wagering business is larger than WATAB and, as a result, the Victorian licence is likely to be a more attractive asset than the WA wagering licence. However, the Victorian retail wagering business is subject to the same challenges from online competition that are facing WATAB and other retail TAB businesses. I also consider that Tabcorp as the incumbent licence holder would have some advantage in any competitive process relating to the retail licence over any other potential bidder, which could create challenges in securing strong competition for the licence through a competitive bid situation. For these reasons, the Victorian government may also not choose to rely on a competitive process to maximise industry funding and the proceeds that it receives in the context of renewal of the Victorian wagering licence.

VIEWS ON THE PROPOSED TRANSACTION

38. I am aware that Tabcorp proposes to acquire all the shares in Tatts via a scheme of arrangement.

39. I am of the view that the merger of the two key totalisator operators in Australia will in no way harm punters, and will in fact deliver material benefits to the racing and wagering industries for a number of reasons, including:

    a. the consolidation of tote operators is long overdue - the historical structure of the wagering industry is not optimally economic or efficient in the current wagering

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environment. Indeed, Australia's federal system, whereby each state or territory government was responsible for legislating and regulating wagering and lotteries, produced a fragmented and ultimately inefficient model of state-based wagering products. The privatisation processes that have occurred in all states and territories other than Western Australia has allowed the wagering industry to operate more efficiently, as tote operators can acquire licences across state borders. From a pari-mutuel wagering perspective, the last step is to consolidate tote ownership, which is critical from efficiency and scale improvement perspectives, and to the long term viability of pari-mutuel wagering in a market with increasingly alternative forms of competition. From my experience at the AFL, I have seen the benefits that national management of a sporting code can bring and consider consolidation of wagering operators an important step in the direction of national organisation of the racing industry;

b. a single tote operator is critical to the survival of the retail limb of the totalisator business model. The totes' retail outlets are under considerable pressure and are declining in market share as punters shift towards using the technology platforms offered by both TAB's and corporate bookmakers. The best way for the totes' retail offerings to compete with corporate bookmakers in the future is through investment at a national level in technology through the retail framework. Greater investment in the visual offerings of retail shopfronts and supporting technology is needed for totes to regain ground on the competitive edge that on-line offers, particularly through corporate bookmakers but also TABs, currently have in this space. This redevelopment of the retail space can really only occur optimally with single ownership of the totes Australia-wide, where such capital investment can ultimately be best justified economically.

40. I consider that the future of the wagering industry will be best served with one national tote operation, providing both tote and fixed odds products through national pools, with competition from three or four corporate bookmakers. I am of the view that this structure would ensure there is sufficient depth in the market in terms of wagering product offerings available to the punter, as well as provide the ability to better achieve appropriate proportionality in the funding to the racing industry between the totes and corporate bookmakers. In addition, the tote pool is optimised as a risk management tool if it becomes a larger, national pool. I consider the proposed transaction is a critical step towards national tote pools for the wagering industry.

41. I am not of the view the proposed merger will reduce bidding competition for retail wagering licences, or that state governments and the racing industry will be worse off as a consequence. Retail wagering businesses are subject to challenges as a result of increasing online competition. Both the racing industry and state governments can adequately protect

their interests by ensuring appropriate funding frameworks are in place when structuring any process around the sale or renewal of a licence. In addition, state governments are in a position to extract greater value from a stronger tote entity in any negotiations, as the merged Tabcorp would be likely to be in a position to place a higher value on state wagering licences, which in turn would deliver increased funding flow throughs to both the state governments and racing industry.

VIEWS ON MEDIA RIGHTS AND THE PROPOSED TRANSACTION

45. During my time at Tatts, it did not have any racing vision broadcast operations. I understand that this is still the case.

46. I am aware some industry participants have in the past had some concerns about the fact that Tabcorp is a tote owner and operator that also has extensive vision rights and Sky channel. However, I am of the view the existing situation with respect to media rights will not materially change as a result of the proposed merger, for two reasons:

    a. First, Tabcorp already has a number of media rights which it broadcasts through the Sky racing television channels and Sky Racing Radio. In my view, this current situation has not proven to distort the wagering media market in any substantive way, nor prevent other entrants as reflected by TVN previously and more recently racing.com. Further, the proposed merger will not change the status quo; and

    b. Second, the introduction of free-to-air coverage of racing via racing.com and Channel 78 in Victoria (a Seven West Media platform) by Victorian Racing has gone some way to reducing the extent of Tabcorp's ownership over media rights, and suggests racing clubs in each state / territory are capable of splitting media rights across different platforms if they so desire, particularly in today's digital world.

47. In my opinion, the link between wagering and vision is critical. As such, a tote operator that has a strong vision offering and broad coverage of vision will ultimately be able to provide punters with a significantly better wagering offer.

48. In the past, splitting exclusive vision rights across different television broadcasters has proven to be problematic for tote providers, venues, punters and ultimately the racing industry. For example, the introduction of thoroughbred racing channel "TVN (Thoroughbred Vision)" in 2005 was extremely inconvenient for the retail totes and their associated venues as they were required to have more television screens showing in retail venues. Punters did not enjoy the fact that only certain races were being displayed on certain screens directed to different broadcast feeds. In addition, the split between vision rights added considerable expenses for TAB venues, who were required to pay two separate sets of rental/broadcast fees. As a result, the fragmentation of vision rights with TVN slowed the growth of retail wagering and

negatively impacted venues, totes and the racing industry. This time around with racing.com the impact is significantly different given the large amount of digital consumption of racing and the less strict television access arrangements to races (and improved product differentiation between television offerings).

49. The most appropriate space for a split of media rights is in relation to digital offerings. In my experience with the AFL, the joint venture arrangement between the AFL and Telstra for the digital viewing platform has been an effective vision strategy which aligns well with the way football games are increasingly being consumed, particularly by the younger demographic. I consider the wagering industry to be analogous to the AFL in that respect, and it is likely to increasingly benefit from digital strategies. In fact, this is already demonstrated by the advent of www.racing.com.

ANNEXURES

50. Set out in Schedule "**A**" of my statement is a table of annexures that I refer to in my statement.

Signature of witness

Ray Gunston, General Manager of Finance, Corporate and Major Projects at the Australian Football League

Date: 24 / 2 / 2017

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SCHEDULE A

TABLE OF ANNEXURES REFERRED TO IN STATEMENT OF RAY GUNSTON

Annexure	Title	Confidentiality
RG-1	Ray Gunston, 'Report on the Potential Privatisation of the Western Australian TAB (WATAB)' (2014)	

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REPORT TO WESTERN AUSTRALIAN RACING REPRESENTATIVE GROUP (WARRG)

ON THE POTENTIAL PRIVATISATION OF THE WESTERN AUSTRALIAN TAB (WATAB)

Prepared by :
Ray Gunston
November 2014

Including Executive Summary

To the Reader,

This Report has been prepared for the Western Australian Racing Representative Group (WARRG) to assist in the deliberations of the WA Racing Industry in relation to the potential privatisation of the Western Australian TAB (WATAB) by the Western Australian Government. The objective of this Report was to explain what privatisation means, to explain how wagering works and how a TAB operates, to describe what a privatisation of WATAB might mean, and to discuss the possible implications for the WA Racing Industry of a potential privatisation of WATAB. It makes no recommendation, and was not asked to, on whether or not the privatisation of the WATAB should occur.

This Report has provided all of these explanations and discussions to the extent possible recognising that this was required to be done outside of Racing and Wagering Western Australia (RWWA) as WATAB sits within RWWA. These matters are covered in detail in Chapters 3-6 of this Report.

The Executive Summary in Chapter 2, together with Chapter 7, provide an overview of those Chapters and suggest some positions and approaches that the WA Racing Industry may wish to adopt in relation to a potential privatisation of WATAB. Major recommendations, proposals, and key propositions have been shaded in the Executive Summary for your clearer reference.

Privatisation of a TAB is a complex matter with many moving parts, I trust this Report helps you understand it better.

Ray Gunston

November 2014

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CHAPTER 1 INTRODUCTION

The Western Australian Racing Representative Group (WARRG) has been formed to represent the interests of racing industry participants in Western Australia in relation to the potential privatisation of the Western Australian TAB wagering business (WATAB). WARRG commissioned Ray Gunston to assist the Group in relation to this matter with the following Terms of Reference and Scope of Work:

1.1 Aim of Engagement

The aim of this consultancy arrangement is to provide advice on what privatisation of a TAB involves, the issues that it raises for Racing Industry Participants, the financial and other implications for the Participants, and to assist the Participants in their engagement with all relevant stakeholders in this regard.

Ray Gunston will work with and provide direction to the Racing Industry Participants in this exercise, and represent them in engagement with, presentations to, and meetings with all stakeholders, including the Premier and Treasurer of the State who are proposing the privatisation.

A major objective is to ensure Racing Industry Participants are able to make informed and considered responses to any request from the Government for them to put the Industry's position(s) in relation to the privatisation of the TAB.

1.2 Scope of Work

The scope of the work to meet this aim of engagement is as follows:

- Explain the concept of a privatisation of a TAB to Racing Industry Participants, including reference to models applied elsewhere.
- Establish a current base-line position of the Western Australian racing industry for communication to industry participants and the Government, covering areas including:
    - the value chain/constituent parts of the industry
    - the financial flows and position
    - current structures
    - the current industry risk allocation of wagering flows
    - the demographics, social perspective and workforce of the industry
    - the infrastructure and asset base situation and investment requirements
- Outline and assess the potential implications to the Racing Industry Participants of a privatisation of the TAB in terms of :
    - industry finances
    - industry structure
    - industry sustainability
    - scenario analysis of potential impacts
- Discuss the different privatisation structures and their differing implications for the Industry and the Government.

- Discuss the impacts of privatisation on country and provincial racing clubs, participants, and communities.
- Set out the pros and cons of the privatisation of the TAB compared to non-privatisation.
- Discussion of the outlook for the WATAB and the Australian wagering industry generally, and its implications for privatisation.
- Consideration of Racing Industry Participants potential stances on their preferred position in the event of privatisation of the TAB in the context of :

  financial commitments/position for the industry

  - no worse off perspective – definition?
  - alternative positioning

  certainty of the level of ongoing racing industry funding

  risk position of racing industry in relation to wagering flows

  operational and capital funding perspectives in this regard

  structure of the racing industry/racing authorities/TAB relationships and financial/product arrangements
- Suggestions on potential strategies the Racing Industry Participants may wish to consider in relation to the potential privatisation of the TAB and the structure of such a transaction, including consideration of matters such as:

  asset consolidation/rationalisation by the Industry

  the racing administration structures into the future

  Racing Industry information generation and presentation to educate all stakeholders on the actual industry economic and financial position.

1.3 Approach

It is currently proposed that the work for this assignment will be primarily conducted in Perth and Melbourne and will include the following activities:

- research and analysis by Ray Gunston as required to undertake the scope of work.
- interviews with relevant West Australian Industry participants, these to include sufficient numbers within each of the following groups to get a materially representative analysis of key issues for each group:

  Breeders

  Trainers

  Jockeys/drivers

  Owners
- interviews with Racing Industry Participant Committee members and/or other relevant racing code representatives, and meetings with the Committee to ensure full coverage of issues and information and to agree appropriate direction. This includes obtaining whatever information Committee members and other officers of the Codes may have to assist with the assignment.
- meeting (if possible) with the Asset Sales Taskforce and with relevant Ministerial Advisors.
- interviews and/or meetings with relevant Board members and executives of Racing and Wagering Western Australia (RWWA) and major race clubs.

CHAPTER 2 EXECUTIVE SUMMARY

2.1 Introduction

The privatisation or sale of a TAB in Australia is a complex exercise with many moving parts and with a range of stakeholders, primarily the Racing Industry, involved in the process and dependent upon the outcomes. This Report raises a wide range of issues and concerns for the WA Racing Industry in any potential privatisation of the Western Australian TAB (WATAB), including in particular the racing industry funding model to ensure the WA Racing Industry is at the least no worse off. The WA Racing Industry cannot support any privatisation of WATAB which does not appropriately address all of these issues and concerns.

If a privatisation of the WATAB is to occur, it is critical that the Western Australian Government has engaged with, and then agreed with, the Western Australian Racing Industry in relation to key parameters of the potential privatisation prior to commencing the formal privatisation process with experienced wagering operator buyers, including experienced buyers of Government-owned gambling assets. This criticality lies in ensuring that the interests of both the WA Government and WA Racing Industry are protected in such a complex tri-partite situation.

2.2 Privatisation of WATAB

WATAB sits within the operations of Racing and Wagering Western Australia (RWWA) and hence currently is not a separate, saleable entity. Privatisation is the process of moving a government-owned business or operation into private sector ownership. This can occur in a number of ways but primarily through sale to a private or publicly listed company. If the WA Government is to sell or privatise WATAB it will need to clearly establish and separate out the exact nature of the wagering operations of RWWA it is actually selling.

It is the wagering operations of WATAB that provide the funds that enable RWWA to make a range of payments in the form of distributions, subsidies, grants, the costs of racing operations and integrity, and other payments to fund the WA Racing Industry. So in forming any view of whether privatisation of WATAB is or is not in the interests of the WA Racing Industry, the Industry needs to consider whether having this wagering operation in the hands of an external private operator will put the WA Racing Industry in a better or worse position than it currently is with WATAB being internal to RWWA, in relation to :

- the amount of funding the WA Racing Industry receives annually from the wagering operations of WATAB
- whether the way in which the amount of this funding would be determined annually will not adversely affect the risk profile of those flows for the WA Racing Industry immediately and into the future
- the security of ensuring such funding is legally guaranteed to the WA Racing Industry
- funding availability in addition to this for WA Racing Industry infrastructure maintenance and development.

These can only be conclusively answered in discussions of the details of a potential WATAB privatisation with the WA Government given that “the devil is in the detail”.

So the WA Government, if it is to privatise the WATAB, will need to put in place a wide range of arrangements including the following in whatever forms that they (after engagement with the WA Racing Industry) may determine (some of which currently exist within RWWA):

- A wagering licence and/or wagering operator's licence for a term to be determined that authorises the wagering operator to conduct exclusive retail tote and fixed odds wagering and perhaps other products under certain conditions and requirements, and contains the racing industry funding obligations (no such formal licence currently exists as RWWA's wagering authorities sit within its own Act).
- The WA Racing Industry Funding Model under which WATAB funds the WA Racing Industry so that the Industry is at the least no worse off.
- The legislative framework under which this new model will operate
- The legal structure under which the wagering operator is to operate – whether it is required to enter into a form of joint venture with the WA Racing Industry or stand alone with or without industry funding arrangements
- A Racing Program Agreement under which the wagering operator and the racing industry determine the annual racing program for the State.
- A Wagering Tax
- Racefield Fee flows and arrangements for the wagering operator
- Arrangements for various financial elements including GST, unclaimed dividends, fractions and other subsidies
- Pooling arrangements, if required
- Arrangements with TAB retail outlets
- Arrangements with Racing Clubs for on-course wagering

2.3 The WA Racing Industry's Proposed Privatisation Position

The requirement for the local racing industry to be paid/funded for the production of its racing product has been encapsulated in all privatisations of TABs around Australia, with specific linkage to, and value and industry funding levels provided for, the exclusive nature of the retail wagering licences provided to the TAB. Such a requirement currently is contained in Clause 50 of the RWWA Act. This payment for use of racing product has also been established in Racefield Fee legislation around Australia. Whilst there is the prospect of arguing over actual ownership of WATAB and the WA Government's right to sell it, and also to raise the question of racing program product rights ownership, it is recommended that the WA Racing Industry not seek these actions if the WA Government, in any potential privatisation process, agrees to and accepts a at the least no worse off racing industry funding model to be met by the new WATAB operator, and to appropriately addressing all the other matters raised in this Report. These must be encapsulated in legislation, licence and contract which link the resulting obligation to fund the WA Racing Industry by the WATAB wagering operator to, and as a condition to the granting of, the exclusive retail TAB wagering licence.

As stated above, this commitment to secured no worse off funding and no worse off risk of the WA Racing Industry must be achieved through engagement with the WA Government prior to any privatisation process of WATAB formally commencing.

The engagement with the WA Government by the WA Racing Industry on this basis would need to deal with a number of concerns about potential privatisation of WATAB. These concerns include :

- the implications of privatisation on WATAB's premium punters and hence WA Racing Industry funding
- similar concerns if a new TAB operator was able to move WATAB account customers to other jurisdictions
- will the new wagering operator have the operational flexibility under its licence to drive revenue through product and process improvement free of bureaucratic delays / restrictions
- appropriate wagering tax settings
- the structures post a privatisation need to ensure the WATAB wagering operator is required to act in the best interest of the local WA Racing Industry.

These and a number of other issues raised in this Report are all matters to be worked through with the WA Government by the WA Racing Industry to ensure the Industry is no worse off in funding and risk profile terms in the event of WATAB being privatised. Without such engagement and appropriate comfort on these issues the WA Racing Industry interests cannot be protected under a privatised model. In this case the WA Racing Industry could not support a privatisation of WATAB.

It is important to address one matter at this point. It is entirely possible to sell/privatise WATAB with essentially all the current financial settings (ie, no worse off) whilst the potential buyer can meet their obligations to their stakeholders. Whilst this will depend upon reasonable price and structural expectations on behalf of the WA Government and the buyer, the buyer should be able to meet shareholder return and taxation payment requirements from the synergy benefits able to be extracted from the purchase. Whilst again "the devil is in the detail", the WA Racing Industry and WA Government should believe there is an ability to constructively engage to achieve acceptable outcomes from a privatisation if that is the direction the WA Government wishes to pursue.

2.4 WATAB/RWWA Performance and Outlook

Given the importance of the funds generated by WATAB to the funding of the WA Racing Industry, the wagering performance of WATAB, in terms of both wagering turnover and net wagering profitability, is an extremely important element in any assessment of the overall performance and operations of WATAB and RWWA. However, RWWA also has responsibility for the critical role of Principal Racing Authority (PRA) for all three racing Codes in Western Australia ensuring the integrity and quality of the racing product is maintained to sustain the WA Racing Industry and to ensure it drives the wagering activities based on this product.

Executive Summary

Over the six year period to 2013 WATAB/RWWA has been the most successful of the larger TABs in the country in relation to turnover growth. It is estimated that this growth figure for WATAB of 39.1% would reduce to somewhere just above 18% if premium customers were excluded from the figures – this is still above the growth rates of TAB's in these other States.

In assessing wagering performance it is important to understand the historical perspective of WATAB and its current situation in the Australian TAB and general wagering landscape. With the challenges of insufficient scale, extended government ownership over longer time periods than other larger and medium sized TAB's, and limited product offers and/or quality of these offerings, leading to less scope to invest in technology advancement, the WATAB previously lagged other TABs.

However, in more recent times WATAB has in essence been catching up in terms of product and technology offers to these other TABs as reflected in its out performance of other Australian TABs in terms of wagering turnover growth. These developments and investments are continuing and suggest that WATAB has the capacity to maintain this out performance for up to five years until the catch up is essentially complete.

This catch up has been made possible through solid management within RWWA of the various factors that have contributed to this performance. Whilst the growth of premium punters turnover has contributed significantly, a number of other improvements in the fixed odds product more recently, ongoing improved retail presentation and product offer, investment in the wagering system and in the digital platform, and improved pooling services and management arrangements have all contributed. Further fixed odds upside, racewalls, and increased self-service terminal rollout will accompany these developments for medium term benefit.

It needs to be recognised that this is occurring within an increasingly competitive wagering environment within Australia, both in terms of increased TAB competition as well as substantial corporate bookmaker growth. WATAB under any ownership structure will be challenged in the future to achieve anything more than the general low turnover/revenue growth outlooks for TABs as retail wagering (particularly pari-mutuel) continues to fall, replaced to varying degrees by generally strong fixed odds growth but at the risk of lower margins.

Accordingly, while the WA Racing Industry has been rightly generally pleased with the funding growth that has flowed from WATAB/RWWA's performance, the "if it ain't broke, don't fix it" argument against privatisation of WATAB needs to be reconsidered in this light. The benefits of, and need for, scale within a larger wagering operation in this wagering industry has clearly been evident in the consolidation of TAB's throughout Australia into the two major Groups – Tabcorp and Tatts.

It must also be noted that these scale issues had led to WATAB/RWWA correctly seeking to pool their pari-mutuel betting with Tabcorp's SuperTAB pool, and outsourced fixed odds pool management to William Hill. However, these pool dependencies are a potential risk longer term, even with existing contracts in place, making considerations such as Racing Industry ownership of WATAB a highly questionable strategy in this instance.

Accordingly, subject to many issues raised in this Report being acceptably resolved, the WA Racing Industry should acknowledge that the privatisation of WATAB is, on balance, likely to occur at some time over the next few years. Even given this situation, the WA Racing Industry should only countenance such a privatisation of WATAB if the racing industry funding model leaves the WA Racing Industry in a at the least no worse off funding position that reflects these past, present and future WATAB wagering performance perspectives. In addition, such countenance should be predicated on governance and licence frameworks that ensure the WA Racing Industry is protected in terms of its risk profile and has a no less favourable standing in the context of a potential privatisation and future wagering licence process outcomes.

It would appear that the focus on this off-course wagering objective growth by WATAB/RWWA has led to a broadly held view, and general agreement, that the racing product integrity, quality and promotion obligations of RWWA's responsibilities have probably received less attention. Reasonable funding growth has generally moderated major criticism in this regard from the WA Racing Industry. Recent actions by and discussions with RWWA indicated acknowledgement and acceptance of the need for greater focus in this regard. Similarly, the focus of WATAB/RWWA on off-course wagering has also resulted in less support to on-course wagering which operates pursuant to the Racing Club on-course licences, contributing along with declining attendances and corporate bookmaker competition to a significant decline in on-course totalisator turnover. This is also receiving more attention from WATAB/RWWA, and is an area of potential growth with or without privatisation.

2.5 The Western Australian Racing Industry - Funding and Value Chains

This Report, with the help of using some data from the IER Report on the WA Racing Industry two years ago, reflects the size, economics, participation and importance of the WA Racing Industry to Western Australia. This Report then delves into the components parts of the funding of the WA Racing Industry, and the value chains of each racing Code in the Industry, to understand the financial models of the WA Racing Industry and its participants.

The funding of the operations of the WA Racing Industry in producing racing animals and racing product is largely provided in an operational sense by punters and owners. Punters who bet with WATAB/RWWA and/or with other wagering operators on WA racing provide the funding base from which WATAB/RWWA meets its obligation to fund the WA Racing Industry. Owners provide the funding to buy racing animals and meet the costs of training and racing these animals to provide the racing product. Whilst each of these sources fund the production and maintenance of the racing animals broadly equally, WATAB/RWWA also meets many of the costs of the administrative and regulatory oversight and integrity of the racing industry and the racing event. Other WA Racing Industry participants obviously invest time, effort and money to achieve appropriate return from these funding sources to sustain their involvement in the Industry.

With this funding context, the overall perspectives to then take from the value chain analysis of the WA Racing Industry are:

- The distributions, subsidies and other payments made to the participants in the WA Racing Industry by RWWA from its WATAB wagering operations have just been sufficient to support the Industry, but on many indicators there has been some significant Industry contraction in recent times.
- Given that the WA Racing Industry has calibrated to the current funding levels, despite increased costs growing faster than returns in most cases, there is no room in the value chains for any less funding from wagering.
- With the punters and owners being the major funders of the WA Racing Industry, and for owners the investment being largely aspirational and seeking intangible returns, any reduction in the wagering contribution to the WA Racing Industry which reduces stakes prizemoney would quickly also reduce owners' investment (based on an acceptable loss context) leading to a higher leverage downwards to racing industry funding than just the distribution reduction.
- The code value chains illustrate that whilst a small number of participants in the Western Australian Racing Industry generate a reasonable return from racing, most are not. It is an Industry in which a small number of people in each segment tend to take a disproportionate share of returns leaving a number to battle financially within the model. In many cases, particularly with owners and some breeders, it is not racing that has created wealth, it is external wealth, and in fact racing tends to reduce this wealth. Racing may often be called a sport of kings, but in most cases it attracts "external" kings, it does not create them in a wealth sense from Western Australian racing.
- Accordingly, there are many in the WA Racing Industry who know nothing else and generate little return but the passion of the Industry. Many employees would have some difficulty finding alternative employment, and operate around minimum wage rates (if that).
- In many cases Racing Clubs survive through voluntary and honorary roles at Board/Committee and operation levels, with Clubs as a whole only breaking even financially on the back of various subsidies paid by RWWA from its wagering returns. Combined WA Racing Club financial figures reflect that there is no capacity to reduce funding to the WA Racing Industry without significantly damaging the financial position and hence potential sustainability of many of Western Australia's Racing Clubs.
- Given the tight operational financial position of the WA Racing Industry, and the need for property holdings availability to breed and train animals for racing, property assets for those who can obtain them become not only operational assets but represent the only form of retirement/superannuation they hold, the value of which is often tied to the sustainability of the industry.

- With its current settings, the WA Racing Industry is effectively just self-funding on an operational cashflow basis, but infrastructure funding to maintain and improve, and keep safe, existing facilities is an ongoing challenge.

Accordingly, the Western Australian Racing Industry currently is somewhat calibrated in a fragile fashion to the current funding structures in terms of distribution, subsidies, the costs of racing operations, and other payments from WATAB/RWWA, whilst the WA Government nets over $40 million per annum from the Wagering Tax.

Any action that reduced funding to this current balanced but fragile situation would therefore clearly very quickly and directly disrupt this position and lead to significant pull backs across the WA Racing Industry as there are no real buffers to absorb any significant reductions in funding. So any racing industry funding model that did not sustain the current funding levels, nor provide some certainty on future funding, would not only immediately impact the WA Racing Industry but would also quickly reduce investment given the hit to confidence it would represent. Some signs of this are already evident from the current uncertainty in the WA Racing Industry from asset infrastructure and TAB privatisation discussions.

2.6 Privatisation Issues and Positions for the WA Racing Industry

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There are a number of issues that the WA Racing Industry needs to take a position on and engage on with the WA Government at the appropriate time in relation to a potential privatisation of WATAB, but many of them can only be determined when the process of potential privatisation is clearer – “the devil is in the detail”. Clearly the principles of “No Worse Off” can be broadly espoused now, and some specific privatisation positions can be established

2.6.1 No Worse Off

2.6.1.1 No Worse Off Funding

The fragile calibrated financial model of the WA Racing Industry as explained in this Report necessitates a “no worse off” funding position as being the current level of distributions, subsidies, incentive/bonus schemes, the racing administration and integrity costs of RWWA, and other payments made by RWWA to Racing Clubs and Industry participants. Going forward, given the comments on the WATAB/RWWA expected medium term wagering performance, no worse off would be reflected in mandated minimum total payment levels to the WA Racing Industry from the WATAB wagering operator over the next five years reflecting the estimated expected WA wagering industry performance in wagering turnover growth from WATAB in a no privatisation scenario. It would be anticipated that this performance could at least be based on an expectation of continuing recent growth rates which have been around 3.5% growth per annum. This will need to be formally assessed through detailed forecasting by RWWA. Of course, this would provide a minimum mandated level of future payments, with better wagering growth performance by a privatised WATAB providing higher payments to the WA Racing Industry. After that time the WA Racing Industry would be exposed to wagering industry performance generally, but should look to a process to review the ongoing WA Racing Industry funding model at that point so that it is based off conditions and performance at that time.

2.6.1.2 No Worse Off Risk

In the context of risk, a funding model such as that proposed above would be a major risk mitigant that would put the WA Racing Industry closer to a no worse off risk profile. The other considerations here are :

- potentially the joint venture model structure for the WATAB and the WA Racing Industry to partially replicate the current RWWA model
- leaving the new “Racing Western Australia” racing / PRA entity with the existing cash reserves of RWWA held to smooth fluctuations in future WA Racing Industry funding that might result from variances in wagering performance.
- provisions within legislation, the licence and/or contractual agreements that require the wagering operator of WATAB to act in the best interests of the WA Racing Industry, and if it does not then the potential for changed terms.

These would need to be discussed with the WA Government in any potential privatisation process.

2.6.2 Other Privatisation Issues

Some commentary on specific areas that are relevant for the WA Racing Industry to consider if WATAB was to be privatised are:

(i) **The Wagering Licence –** that it is an exclusive retail totalisator licence for pari-mutuel and fixed odds betting, with an obligation to meet WA Racing Industry funding. If it is to be a long term licence the WA Racing Industry should look for the licence to include shorter term review points to test the appropriateness of the racing industry funding model and operation of the licence – either through shorter exclusivity terms or similar trigger points. The WA Racing Industry would prefer to see a flexible and timely approval process for products and channels within the licence to obtain a wide product range that drives revenue for the wagering operator.

(ii) **The Legislative Framework** – the major focuses here for the WA Racing Industry are**:**

- That the legislation and licence requires the wagering operator to enter into a contractual funding model with the WA Racing Industry
- That the legislation incorporates a no worse off (or no less favourable) requirement on any licences into the future (including this one) for the WA Racing Industry if privatisation occurs
- That the legislative framework is not too restrictive on the operations of the new wagering operator to ensure that returns are not inhibited

(iii) **Structure –** it is too early at this stage to suggest a preferred WA Racing Industry position other than to state that a model under which the Government and not the wagering operator funds the industry must be avoided. Racing Industry ownership of the WATAB is not recommended.

(iv) **Racing Industry Funding Model –** other than the requirement for the WA Racing Industry to be "no worse off" in relation to funding, the matter of the appropriate model cannot be determined at this stage. Total reliance of a profit share model is however not recommended. Many other aspects of the potential privatisation need to be understood before a view on the desired racing industry funding model can be formed.

(v) Racing Program Agreement – other aspects such as structure will heavily influence how the Racing Program Agreement process is to work, but it requires an integrated Tri-Code grouping for the WA Racing Industry (which Racing Western Australia – RWWA without wagering – could bring given its existing in-house capabilities).

(vi) Wagering Tax – this is a WA Government issue other than it reduces the amount of funding available to the WA Racing Industry, but it is important for the new wagering operator and the WA Racing Industry to get certainty around this matter longer term to lock away the appropriate racing industry funding model into the future.

(vii) Racefield Fees – a "no worse off" position in relation to racefield fees at present is unclear but would probably involve the wagering operator offsetting payments against the WA Racing Industry funding and Racefield Fee income flowing to the WA Racing Industry. It is recommended that this offset mechanism for the new wagering operator under a potential privatisation be limited to no more than the amount of incoming Racefield Fees received by the WA Racing Industry each year.

(viii) Other Financial Arrangements – matters such as GST reimbursements, Fractions and Premium Player Rebates will sit with the WA Government and a new wagering operator to agree if a privatisation was to occur, but outcomes would need to be considered in finalising the Racing Industry Funding model. It would be recommended that unclaimed dividends on racing be paid to the WA Racing Industry after the 7 months as set in legislation at present.

(ix) On-course Wagering Arrangements – this is an area that has lacked focus by RWWA up until recently, and an area of some potential upside to all under any future models. Accordingly, this is an area, particularly for Racing Clubs, but also the entire industry, that would need to be dealt with appropriately in a potential privatisation, including consideration of the suggested improvements listed in Section 6.2.1.1.1 of this Report.

2.7 Other Considerations for the WA Racing Industry

2.7.1 WA Racing Industry Governance in a Privatised Model

A refocused RWWA without wagering (Racing Western Australia) could effectively continue to operate the PRA functions as currently. The Tri-Code representative body structure appears to have worked reasonable well. This should also help the WA Racing Industry meet its many challenges by giving it the opportunity to act as a Sport rather than Codes.

2.7.2. WA Racing Industry Asset Infrastructure Efficiency / Rationalisation

With little or no capacity to fund infrastructure maintenance and development requirements across the WA Racing Industry from its operational cashflow break-even situation, it is critical that the entire WA Racing Industry be prepared to address the issues of improved efficiency and rationalisation of infrastructure to sustain the WA Racing Industry in an integrated fashion.

The WA Racing Industry must pursue funding alternatives for infrastructure in any potential privatisation process (or even if it does not occur), but to have any success in this it needs to commit to pursuing such efficiency / rationalisation processes.

2.7.3 WA Racing Industry Engagement with the WA Government Over Potential Privatisation of WATAB

The objective for the WA Racing Industry if the privatisation of the WATAB does proceed is to be able to engage with the WA Government early in its process deliberations to work with and agree with the Government the acceptable positions on the many issues of a privatisation that have been outlined in this Report. It is recommended that the WA Racing Industry seek such engagement and interaction with the WA Government prior to any formal discussions or processes commencing with potential bidders and/or a formal sale commences.

To ensure that the WA Racing Industry's, and the WA Government's, best interests are met in the privatisation process, it is critical that the Government is very clear on the objectives to be achieved in the privatisation/sale for the WA Government and the WA Racing Industry, and on funding models, structures, key licencing parameters and legislative and contractual frameworks to present to potential bidders. Where relevant, these will have been agreed with the WA Racing Industry and formally documented as the basis for seeking proposal bids from potential bidders in such a potential privatisation.

In this context, the Western Australian Racing Representative Group will need to obtain a mandate from the WA Racing Industry to undertake such discussions with the WA Government, and seek a commitment from the WA Government for such engagement at the front end of a potential privatisation process. Such engagement must come with a requirement for obtaining agreement between the WA Government and WA Racing Industry on the relevant industry issues identified in this Report for a potential WATAB privatisation.

This early engagement and agreement on positions for a WATAB privatisation between the WA Government and the WA Racing Industry is considered to be the best risk mitigation strategy for the "sellers" when dealing with experienced wagering operators, and some who have also been involved in previous privatisation processes.

It is particularly important for the WA Racing Industry to have a clear and documented commitment with the WA Government on the privatisation framework. Such a process occurred within the 2012 wagering licence bid process in Victoria, based on the no less favourable (ie, no worse off) requirements within the legislative licencing provisions surrounding the new licence.

CHAPTER 3 Explaining the WATAB, RWWA and Privatisation

This chapter explains the background and operations of the Western Australian TAB, (WATAB), and then briefly explains what privatisation is, outlines relevant Australian examples of privatisation and how they occurred, and sets up the basis for determining the potential implications for WA Racing Industry participants of a privatisation of WATAB.

3.1 The West Australian TAB (WATAB)

3.1.1 History

The Western Australian Totalisator Agency Board (WATAB) commenced operations in 1961 as a public authority under the Totalisator Agency Board Betting Act 1960 to replace the approximately 206 licenced off-course betting shops, legal in Western Australia since 1958. The initial TAB was established through assistance in funding from the thoroughbred and harness racing codes. Betting was expanded to include greyhound racing with the introduction of such racing to Western Australia in 1974.

The WATAB continued to expand its bet types, including the introduction of fixed odds sports betting in 2000, and hence to grow its wagering turnover. In 2001 the Government received a report called Future Governance of the Western Australian Racing Industry – A Report to the Minister for Racing and Gaming, October 2001 – a study commissioned by the Minister to be conducted by the Western Australian Racing Industry Review Committee, at the end chaired by Mr. R. H. C. Turner, to examine the entire racing industry (the Turner Report). An outcome of the Turner Report was the introduction of Racing and Wagering Western Australia (RWWA) in August 2003, and the transfer of WATAB's wagering responsibilities to RWWA in January 2004 (at which time the Totalisation Agency Board ceased to exist of a legal entity).

RWWA currently operates the wagering activities under the TAB and TABtouch brands as the primary and online brands respectively, through its Marketing and Retail Divisions with support provided by the corporate support divisions of RWWA. Racing Operations and Racing Integrity are also responsibilities of RWWA and are performed through the Racing and Racing Integrity divisions of RWWA. The structure of RWWA is outlined in the following section.

3.1.2. RWWA

RWWA is a body corporate (and <u>not</u> a public authority) and operates under the Racing and Wagering Western Australia Act 2003 (the RWWA Act). RWWA is <u>not</u> a Crown agency, is not subject to Ministerial direction, and is not a public sector body. For appropriate accountability reasons it is subject to the Financial Management Act 2006, reports to Parliament, and is required to submit certain plans and information to the Minister for approval. The RWWA Act established RWWA as the controlling authority for thoroughbred, harness and greyhound racing in Western Australia, together with the responsibility for off-course TAB wagering (on-course wagering licences are held directly by the Racing Clubs). This happened in two stages.

Effective 1 August 2003, RWWA assumed the principal racing club/controlling authority responsibilities of the Western Australian Turf Club, the Western Australian Trotting Association, and the Western Australian Greyhound Racing Authority. On 30 January 2004, as indicated above, the Totalisator Agency Board Betting Act 1960 was repealed and RWWA assumed responsibility for the conduct of off-course TAB wagering.

The structure through which RWWA undertakes these responsibilities is as shown in Chart 3.1.2 on the next page, with a number of divisions overseeing its various activities:

CHART 3.1.2

BOARD

CEO

Commercial	Marketing	Retail	Racing Integrity	Racing	Information Services	Finance and Business Services	Human Resources
• Major contract negotiation and structuring • Broad industry intelligence and monitoring • Key strategic interfaces • Commercial assistance on strategic and major operational initiatives.	• Responsible for Internet, Mobile and Call Centre Channels, all wagering products, and management of RWWA's premium business. • Manages marketing, advertising, and promotion, social media and Loyalty CRM activities • Manages wagering brands • Racing Radio and TABForm publication	• Responsible for the retail TAB network • Interacts with 319 agencies (as at 2012/13) throughout the network	• Responsible for all matters pertaining to proper conduct and integrity of racing in WA • Includes stewards from all three codes and Racecourse investigators	• Responsible for racing operations • Activities include - fixture planning - racing systems and information maintenance - handicapping and grading - stakes supervision - vision contracts - major event support - overall strategic directions of the racing industry in WA.	– Provides technical, consulting and support services for delivery of wagering services – Technical support for: - All RWWA wagering and racing information systems - Data communication network - Ticket machines - Information security - Racing Radio - All wagering related technical infrastructure	– Responsible for - financial management and strategy, - Risk and business continuity systems, - Wagering compliance - Audit and legal matters - Administration of licencing and registration - Business intelligence functions	– Responsible for : - Development and implementation of HR management - Management of workplace and employee related functions - Supports managers on recruitment, induction, performance management - Payroll services

3.1.3 **Ownership of the TAB**

In discussions around many of the privatisations of TAB's throughout Australia over the last three decades the question has been often asked as to the actual ownership of the TAB, the potential to argue beneficial ownership by the Racing Industry, and the ability of a Government to "sell" the TAB in a privatisation. As will be discussed later in the sections on privatisation in this Report there are many models as to the form of privatisation and what this can mean in terms of the structure of the privatisation or sale.

Whilst legal opinion could be sought to obtain more precision to this question in the case of WATAB, it would appear that any challenge to the ability of the Government to sell WATAB would be significantly problematic and the likelihood of success highly uncertain. Key matters/assets in the value and operation of a TAB, as are more fully explained in Section 6.2, are the infrastructure, networks and contractual arrangements underpinning the actual wagering operations of the TAB, the licence/authority/permission or similar granted ability from the Government to legally operate a betting agency (particularly an exclusive retail-based TAB operation), and access to the product on which the wagering is conducted - that including the race program, the races, the animals, the numbers, and the vision of the racing event.

Accordingly in any consideration of ownership and/or ability to sell or privatise, it is the ability to transfer these three value drivers to another party for consideration that would appear to largely determine the answer. In this context it would appear that the Racing and Wagering Western Australia Act 2003 confers all these to RWWA in that the Act confers on RWWA the ability to conduct off-course wagering (in effect the "licensee"), in accordance with this "licence" RWWA is permitted to own terminals and enter commercial agreements to undertake this off-course wagering, and as indicated above is the controlling authority and assumed the principal racing club/controlling authority responsibilities for the three codes, thereby owning and therefore ensuring access to the product on which wagering is conducted.

It would therefore appear that particularly with the last of these factors also sitting with RWWA and not specifically or by default with the WA Racing Industry, there is limited ability for the Industry to argue any rights to ownership of WATAB and/or RWWA. However, as it would appear that perhaps this issue has never been fully tested legally, and given the manner in which the WATAB was established and funded, there is some uncertainty as to the outcome of a challenge to WATAB ownership, however unlikely. This issue would best not be pursued, given its propensity to be both a long drawn out court case and potentially very expensive for all parties, if the Western Australian Government appropriately engages with the Western Australian Racing Industry early in any potential privatisation of WATAB to agree the parameters that protects the funding and sustainability of the Industry if such a privatisation eventuates.

In a related and probably more positive context, it is however in the same section of the RWWA Act which confers the functions and powers of RWWA in relation to gambling (Part 5 – Specialised functions in relation to gambling), and particularly Clause 50, that the Western Australian racing industry needs to focus its attention. That is Clause 50(c) which requires RWWA as part of its gambling function:

"to develop and implement a scheme for the distribution of net profits and to negotiate funding agreements with individual racing clubs".

It is under this clause that the current distributions, subsidies and other payments to WA Racing Industry participants and to Racing Clubs are made annually by RWWA.

The key linkage created here, and recognised within this Clause 50, is that of the exclusive nature of the retail off-course wagering licence being linked to the requirement and obligation to fund the WA Racing Industry. That is, the quid pro quo of getting such exclusivity, which is an extremely valuable asset to the wagering operator, given that retail turnover represents over 60% of WATAB/RWWA's total turnover, is to take on this WA Racing Industry funding obligation. In any potential privatisation of WATAB, such exclusivity (which currently sits with WATAB) will therefore need to be linked to WA Racing Industry funding obligations through the legislative and licencing processes, encapsulating a no worse off position for the Industry in this regard.

This exclusivity is what gives value in the privatisation of a TAB in terms of the proceeds of sale and accordingly has been a critical element of all TAB privatisations. The no worse off (or more specifically the no less favourable) provisions for the Industry Funding Model is a feature of the enabling Victorian legislation.

The ability to grant and enforce retail exclusivity clearly sits with the Government within the wagering licence framework and is therefore a fundamental provision of the licencing process within a potential privatisation. As discussed, with such exclusivity and therefore the ability to generate the profitability that such exclusive access gives to the wagering operator, the wagering operator is required to accept the obligation to fund the local racing industry under what is essentially a tripartite arrangement between the Government, the racing industry and the wagering operator.

If a privatisation is to occur, the RWWA Act will need to be amended in a number of areas to deal with the different ownership model and the matters outlined above, and more particularly this Part 5 of the RWWA Act. Therefore, what happens to Section 50(c) in any potential privatisation process is of particular focus for the racing industry. This is discussed in more detail in various parts of this Report, and particularly in Section 5.2.2.1.

3.1.4 **The Operations of the WATAB**

So to be entirely clear, the WATAB does not actually exist as a separate entity and is part of RWWA. As outlined above it operates through various business divisions of RWWA. Under the RWWA Act, the actual functions in relation to gambling of RWWA are essentially:

(i) ensuring on-course wagering by bookmakers and racing club totalisators is conducted in accordance with the Betting Control Act 1954.

(ii) to operate an off-course totalisator wagering service on races and certain sporting and other events

(iii) to operate on-course totalisator wagering services for racing clubs when requested by the clubs

(iv) to operate a fixed odds wagering service in relation to races and certain sporting and other events.

These are the TAB-type activities currently performed by RWWA, with the obligation for them to then satisfy section 50(c) as outlined above in relation to distributions to the WA Racing Industry.

The first of these functions outlined above in (i) is a compliance and regulatory oversight function that does represent an actual gambling activity by RWWA itself and hence does not form a function that would represent a TAB activity, and would not form part of the functions that may be privatised. It is a wagering integrity responsibility that would be expected to stay under WA Government ownership.

3.1.4.1 **Pari-mutuel Betting**

The activity covered under (ii) and (iii) above as an off-course totalisator wagering service and for on-course tote service provision represents what is called pari-mutuel betting. Pari-mutuel betting is a betting system in which all bets of a particular type on a specific event are placed together in a single pool. A prescribed percentage of that pool is to be paid back to winning bets (the prize pool) with the rest retained by the TAB as a commission to pay taxes, meet its costs, and to pay other requirements such as WA Racing Industry distributions in the case of RWWA. Accordingly, as the pool grows from the bets being placed the amount available to be paid for winning bets grows. The TAB is able then to display the potential dividends (winning bet payouts) that could be paid <u>at that time</u> for the bets placed at that time for each alternative result if the race or event occurred at that moment. This is determined by dividing the prize pool by the amount of bets on each outcome assuming that is the winning outcome. As time progresses until the race or event occurs and further bets are placed these different outcomes and the possible dividends keep moving with the amounts of bets into the pool and with the relative amounts bet on the different outcomes. This continues until bets can no longer be received when the race or event commences, at which time the actual dividends (prize payout) will be determined upon receipt of the results of the race or event. Therefore under this form of betting the punter does not know the prize dividend they will actually receive until after the race or event has finished irrespective of when they placed the bet.

Pari-mutuel betting of this type is only provided by TAB's in Australia, and therefore is either know as TAB or Totalisator or Tote betting in this country. As will be explained in Section 4.3.2 of the Report, a number of corporate bookmakers in Australia do offer products called Best Tote (TAB) Odds – they are essentially re-selling TAB dividends, not running a totalisator pool.

Accordingly in pari-mutuel betting the totalisator receives the set percentage of all bets placed and its return is not affected by the result due the dividend payouts being determined by the final amount of winning bets being divided into the prize pool.

These pari-mutuel approximate dividends leading up to a race, and the final result dividends actually payable after the race, are those that are displayed on screens throughout retail TAB outlets, race tracks and through internet and mobile devices in respect of Tote or TAB odds for WATAB, Victorian (known as SuperTAB or S-TAB), NSW or Tatts, which are the four totalisator pools operating in Australia.

So in the case of WATAB this pari-mutuel betting is conducted for all off-course betting through the various channels of retail, self-service terminals, internet, mobile devices and phone betting by RWWA directly. On-course pari-mutuel or tote betting in Western Australia is currently also coming into the WATAB pool but on behalf of the Racing Clubs who hold the totalisator wagering licence in relation to such betting on their course on race days.

3.1.4.2 **Fixed Odds Betting**

In contrast to pari-mutuel betting, fixed odds betting is a form of wagering where the punter receives and retains the odds that have been quoted to them at the time when they place the bet. Irrespective of any subsequent change in the odds that may be provided to other punters for the same type of bet the odds provided to the original punter will be what they received at the time of placing their bet. Accordingly, unlike pari-mutuel betting, punters who therefore bet on the same outcome will receive varying odds on which they will receive different prize dividends if their outcome is a successful outcome. In this case the wagering operator (bookmaker) will actively price and adjust the odds in an attempt that they make a profit irrespective of the actual outcome of the race or event (although this may not always be possible). So in this case the fixed odds will vary leading up to the race or event as the wagering operator seeks to “manage” the book, but if a punter has previously placed a bet with the bookmaker the punter’s dividend remains unchanged if the bet is successful.

Accordingly, in this type of betting the wagering operator is not assured of a commission or a profit, with profitable outcomes for the wagering operator dependent upon their skills at managing this risk within the book for the range of probabilities of different outcomes. The wagering operator is therefore putting its own money at risk in this situation, and fixed odd betting for a wagering operator is therefore more risky than totalisator betting for the operator, as the profit margin is not guaranteed and can vary significantly across each outcome. This risk is somewhat mitigated by the wagering operator offering such betting on many types of races and events to diversify their risk across a wide range of different propositions (similar to diversifying stock market equity investment risk through holding a wide portfolio of different company shares).

3.1.4.3 **WATAB Betting**

In accordance with its enabling legislation, RWWA conducts both of these forms of betting under the TAB and TABtouch brands. The pari-mutuel betting or totalisator betting pricing appears under the WATAB pool pricing on screens and devices. The key management considerations in operating a totalisator pool are:

- the wagering or betting system – ensuring it accurately and efficiently records and processes all bets received and automatically ensures accurate pricing of prize dividends up to and following the race or event.
- the size of the total betting pool and therefore of the prize pool – major considerations flowing from the size of the pools are:

— betting pools need to be large enough to allow the totalisator operator to receive sufficient commission to meet the high fixed costs of providing totalisator betting and to meet taxes and, in WATAB/RWAA's case, the distributions and other funding to the WA Racing Industry.

— the size of the resulting prize pool needs to be large enough to ensure that the prize dividends for punters are:

(i) of sufficient magnitude to encourage all punters to continually bet into the pool.

(ii) not subject to overly wide fluctuation or potential manipulation by a small number of large punters to the detriment of all other punters.

This perspective obviously needs to be considered across the entire operation, but also needs to be monitored on a per race or event basis to avoid too many such possible instances (although it is largely unavoidable given some races or events will obviously be less interesting to punters).

- to provide these pool sizes it is important to enable punters to be able to bet into the relevant race or event pools easily and for time periods as early as possible prior to the race or event, and through whatever medium they wish, be it retail off course, self-serve terminal, on-course, call centre, internet or various forms of mobile devices.

Whilst an assessment of how successful WATAB has been in achieving these outcomes will be discussed later, its approach to addressing these tote pool size issues has been to enter into a long term pooling agreement with Tabcorp under which the pari-mutuel bets put on with WATAB essentially all get added into the SuperTAB pools operated by Tabcorp in Victoria and successful punters receive the prize dividends that are determined and paid from those racing pools, which in 2013 was around $5.5 billion in total. This enables WATAB to provide its punters with the magnitude and integrity of the dividends that flows from the punters being able to bet into sufficiently large totalisator pools in the vast majority of instances. (Products not pooled include Favourite Numbers, tipping, Footo, some country WA races, and some international races).

For fixed odds betting as explained above, whilst size of pool is an important management consideration for the wagering operator, it is critical that the bookmakers who are setting the prices that are being offered are carefully managing the probability risk of each race or event pool so that any outcome will not cause the wagering operator to in fact lose money and therefore be faced with the need to fund the pool deficit.

As each punter has locked in their odds and potential prize dividend if successful under fixed odds betting, the punters concern is not to the volatility or magnitude of their potential prize dividend as with the Tote, but just ensuring the wagering operator has sufficient funds to pay the prize dividend. Subject to getting the price setting managed right, the spread and overall size of betting in a particular fixed odds pool will generally assist the wagering operator to achieve appropriate outcomes for them and the punters.

The key management factor is however, the ability of the bookmakers of the wagering operator who are managing each book/pool for each race or event to effectively price and risk manage that book/pool to provide fixed odds that attract betting across the field of participants whilst ensuring a profitable outcome for the wagering operator.

In relation to WATAB/RWWA's fixed odds betting offer, RWWA has elected to not attempt to build this bookmaking competency internally but to outsource this to existing fixed odds wagering operators who already have the infrastructure and people to undertake this fixed odds pool management. This has been outsourced over the last few years to various providers. Initially such services were provided by Tabcorp, and then Sportingbet, Centrebet, and now is undertaken by William Hill pursuant to a Management Agreement between RWWA and William Hill.

3.1.4.4 **WATAB Betting Channels**

There are various channels through which punters can place a bet (either pari-mutuel (Tote) or fixed odds) with WATAB/RWWA. These Channels are listed and explained below:

- Licenced Outlet – Pubs – TAB's located within hotels which can be either full service operator terminals with personnel behind the pub counter providing tickets from the terminals and collecting and paying bets and dividends, or self-serve terminals, or both
- Shop front retail TAB outlets – these full service shops offer the similar betting experience as for betting in a licenced premises (minus the liquor licence) with betting terminals at the counter with personal service behind the counter, and self-service terminals. These shops operate under various models with RWWA ranging from agency arrangements, through assignable licencing, to some being directly operated by RWWA.
- Self-service terminals – these are punter operated betting terminals connected to WATAB/RWWA's wagering system located at TAB outlets and on-course that enable the punter to place his/her own bets and feed cash into the bill acceptor contained in the terminal. Accordingly, the punter does not need to go to the counter to use a terminal operator to place a bet.
- On-course – full service operator provision similar to the retail outlet experience with a number of courses having self-service terminals. In this case the punter's bet is going into the WATAB pool and system, but the bets are effectively being placed under the relevant Racing Club's own on-course totalisator licence as opposed to all of the off-course bets being under RWWA's betting authority.
- Call Centre – subject to opening a betting account with WATAB/RWWA punters are able to call an operator at the WATAB call centre and put a bet on over the telephone by verbally telling the operator the bet the punter wishes to place. In addition, RWWA has Interactive Voice Recognition (IVR) where no operator exists but the bet is taken by an electronic system from the call.
- Internet – again subject to opening an account with WATAB/RWWA punters are able to place a bet via an individually password controlled access to the punter's account through the TABtouch website. This can be done through any internet enabled device.
- Interactive TV – with an account punters are able to place Tote bets through the TABtouch website via interactive TV.

- Mobile Wagering – subject again to having opened an account with WATAB/ RWWA punters are able to place bets via their mobile telephone and/or mobile tablet device through TABtouch apps.

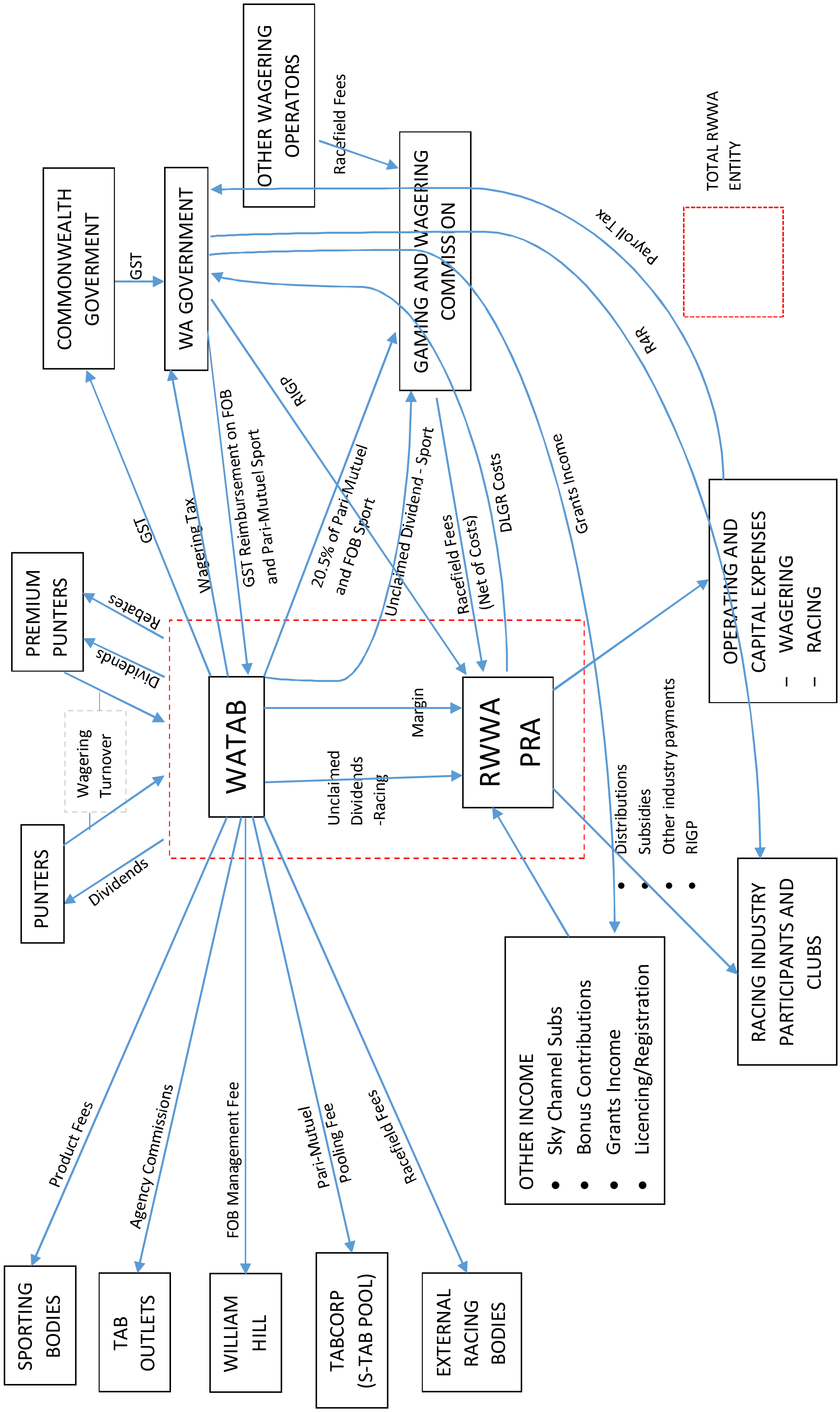
3.1.4.5 The Operational Financial Flows of WATAB/RWWA

As the WATAB business is embedded within the operations of RWWA there is an intermingling of operational cash flows that would be considered to be related to TAB activities and operational cash flows that would be considered to be related to racing industry integrity, operations and promotions activity in its role at the Principal Racing Authority (PRA).

Chart 3.1.4.5 on the next page contains a diagram that sets out the cash flows of RWWA in respect of both of these activities. These flows are explained in some detail below:

1. **Wagering Turnover from punters -** the total amount of wagers bet with the WATAB on all types of pari-mutuel and fixed odds betting. For the 2013/14 financial year it is expected that this turnover will exceed $2.2 billion (of which less than 1% is on-course). Pari-mutuel (Totalisator) betting represent approximately 81% of this total turnover (almost exclusively racing), and fixed odds around 19% (of which just over 62% is racing wagering with the rest on sport).
2. **Wagering dividends** – payments made to punters from the pools formed by their wagers in relation to winning bets. In the pari-mutuel pools, with minor variations for channel types and bet locations the proportion of dividends paid out of turnover bet is around 79.82%. Whilst as explained above the gross margin on fixed odds betting for the wagering operator is not fixed as for pari-mutuel betting, it is believed the WATAB achieves a gross margin of around 14% of turnover on its fixed odds betting.
3. **Pooling/Management Fees** – as explained above, WATAB doesn't operate its own pools except for a few products outlined in Section 3.1.4.3. In the case of pari-mutuel wagers with WATAB most of these are combined into Tabcorp's SuperTAB pools and pooling fees are paid on a percentage rate of WATAB's pooled wagering turnover. In the case of fixed odds betting the bets are managed by William Hill within its systems as separate WATAB pools, for which a management fee is paid to William Hill based on a percentage of the gross margin generated. These fees together are understood to have totalled over $18 million in 2012/13.
4. **Goods and Services Tax (GST)** – WATAB/RWWA pays GST to the Commonwealth Government. The GST is paid on WATAB's wagering margin. This amounted to $26.85 million in 2012/13.
5. **Commonwealth Government GST Distribution** – through the Commonwealth / State financial arrangements GST collected by the Commonwealth Government is distributed to the State Governments.

CHART 3.1.4.5 - RWWA FINANCIAL FLOWS



6. **GST Reimbursement** – the Western Australian Government provides WATAB/RWWA with a reimbursement of GST paid on the fixed odds betting margin and the pari-mutuel sports margin. It is understood this represented around $2.3 million in 20212/13. Wagering tax rates on racing were reduced in 2007 to the extent of the GST applicable and the rebate on this betting was therefore eliminated.

7. **Wagering Taxes** – the Western Australian Government levies wagering taxes on the WATAB/RWWA as defined under the RWWA Act. The current tax rates are outlined below:

   - a tax on pari-mutuel sports wagering turnover levied at 5 percent of turnover
   - a tax on fixed odds sports wagering at 0.5 percent of turnover
   - a tax on fixed odds racing wagering turnover levied at 2 percent of turnover
   - a tax on off-course racing wagering turnover levied at 11.91 percent of gross margin (a taxation concession rebate applies for premium punters)

   In 2012/13 the total wagering tax paid was $40.42 million of which $37.71 million was taxes paid on margin (ie, pari-mutuel racing)

8. **Product (Racefields) Fees Expense –** WATAB/RWWA pays product fees to interstate and international racing industries so that it can publish interstate and international racefields and take wagers on these interstate and international races. The various product (racefields) fee structures in each Australian jurisdiction are outlined in Section 4.4.1. In 2012/13 it is understood that these international and interstate product fees totalled around $33.3 million (including on-course fees).

9. **Product (Racefields) Fees Received –** on the same basis, the Western Australian Government has legislated under the Racing Bets Levy Act 2009 and associated Regulations to prescribe a levy to be paid by betting operators betting on WA races and determine and prescribe the amount of the levy. The Western Australian Government receives the levy via the Gaming and Wagering Commission and under the Gaming and Wagering Act has determined at present that these be paid through to RWWA (net of administration costs of the Commission) for distribution to Racing Clubs. The amount believed to have been received by RWWA in this respect in 2012/13 was around $31.1 million.

10. **Sports Wagering Account -** under the RWWA Act the WATAB/RWWA is required to pay 25% of its margin (after wagering tax) on pari-mutuel and fixed odds sports betting to the Sports Wagering Account held by the Gaming and Wagering Commission (reported by RWWA as Distributions to Sport).

11. **Unclaimed Dividends –** winning dividends that punters have not collected after 7 months from the date of the race or event are released from the prize pools of RWWA and, in the case of sports bets are paid to the Sports Wagering Account in the Gaming and Wagering Commission (reported by RWWA as Distributions to Sport), and for racing go into RWWA's general funds for distribution. Unclaimed dividends usually represent about 0.4% of total dividends, and in 2012/13 provided RWWA with $8.25 million in racing unclaimed dividends as income.

12. **Fractions –** dividends may be rounded down to the nearest 5 cents and any proceeds of this flows to RWWA general funds in accordance with Section 60(3) of the RWWA Act. It is understood that this represents around 0.8% of pari-mutuel racing turnover. This is partly offset by adjustments for minimum dividends and the like which would suggest these matters represent around $10-11 million of net funding for RWWA annually.

13. **Premium Customer Rebates –** turnover volume rebates are provided to large (Premium) punters given the amount of betting business they provide. These are partly funded by wagering tax reductions on this particular turnover.

14. **Distributions to Racing Clubs and Sports Organisations –** distributions, grants and implicit subsidies are made to the racing industry and to the sports industry by RWWA, essentially all funded out of the operations of the WATAB. RWWA provides distributions in accordance with its current distribution model (which will be discussed further throughout this Report). Total distributions for the 2012/13 and 2013/14 years were $117.67 million and $124.19 million respectively allocated as follows:

	2012/13	**2013/14**	
Thoroughbreds	$ 69.02 m	$ 73.61 m	
Harness	$ 29.77 m	$ 30.36 m	
Greyhounds	$ 14.88 m	$ 15.77 m	
Sports	$ 4.00 m	$ 4.45 m	(see 10 and 11 above)
	$117.67 m	**$124.19 m**	

RWWA provided Grants and Subsidies in addition to these distributions of $2.19 million and $11.04 million in 2012/13 and 2013/14 respectively. RWWA also provides a number of sponsorships to Clubs ranging from $20,000 to $100,000.

15. **Agency Commission –** retail TAB outlets operate under various business and financial arrangements with WATAB/RWWA in terms of being a distribution channel for wagering. Commissions are paid to these operations which in 2012/13 generated around $33.4 million in payments made to these outlets.

16. **Other Income –** in 2012/13 this was around $9.5 million and is understood to comprise a variety of income sources including charges from Sky Channel subscribers (Pubtabs, etc), racing licencing and registration fees, grant monies from the WA Government such as for the R4R and RIGP grants programs, and various recoupments.

17. **Product Fees -** fees are paid to other sporting bodies including the AFL and Tennis Australia for wagering on their sporting product. These fees amounted to $0.9million in 2012/13.

18. **Costs of operation –** RWWA incurs operating and overhead costs for conducting its wagering business, in its role of providing governance to the wagering and racing industries, and in the various other functions that flow from its role of the Principal Racing Authority in Western Australia, including payroll tax paid to the WA Government of around $2 million per annum. As these roles use a variety of support services as well as have dedicated staffs and divisions, it is difficult to precisely split up the total operating cost of an estimated $128 million in 2012/13 between these roles. It has been roughly estimated that the costs of the wagering business (with some allocated cost) is in the vicinity of $100 million.

    It should be noted that of these RWWA operating costs there is over $800,000 per annum paid to the Gaming and Wagering Commission and the Department of Racing, Gaming and Liquor to defray their costs.

3.1.4.6 The Capital Financial Flows of WATAB/RWWA

Outside the specific capital expenditure on the wagering system and any retail network related expenditure, the WATAB operation has little call on capital expenditure requirements.

Capital funding has in the past been sought for industry infrastructure funding requirements from the Western Australian Government through business cases put to the relevant Government Departments by RWWA. At present (until 2015) the Western Australian Government is providing funding through RWWA under the Racecourse Infrastructure Grants Program for Race Club investments in infrastructure, and also providing matching funding for some of the regional investments through the Royalties for Regions program.

RWWA provides no other specific capital funding, focusing on its annual distributions from its operations to the Racing Clubs and Industry Participants. Some limited investment in training facilities and the like are made occasionally.

3.1.4.7 The Current Financial Situation of WATAB/RWWA

As outlined above, without having the ability to fully review and analyse the detailed accounts of RWWA, it is not possible to completely separate out the WATAB's results from the overall RWWA results. However, in overall terms, when looking at the annual operating flows of RWWA, essentially RWWA generated most of its income from the TAB operation, supplemented by the Product Fees received via the WA Government and the GST Reimbursement by the WA Government on Fixed Odds Betting and Pari-mutuel sport. After paying Wagering Taxes to the WA Government, costs of TAB sales including pooling/fixed odds management fees, product fees and rebates, and operating costs for the TAB and Racing Services, the balance is available for Distributions and other funding of the WA Racing Industry. RWWA distributes most of this annually, with some profit retained to provide cash balances as a reserve buffer should the TAB operations in a particular year not generate sufficient profit to allow racing industry funding to be the same as or increase on the previous year. (Cash is also retained for future wagering and racing capital expenditure requirements).

The 2012/13 financial performance of RWWA has been restated in a different format below from the Statement of Comprehensive Income in its Annual Report to attempt to better show its inflows and outflows.

Item	$M	$M	$M
Inflows			
Wagering Margin			
(net of GST)		315.741	
Grant Income			
• Government Grant	0.561		
• Racefield Fees	31.123		
• Racing Infrastructure Grants Program	0.207		
• GST Reimbursement	2.296	34.187	

Unclaimed Dividends – Racing		8.253	
Racing Services – other revenue		4.749	
Other Revenue		4.778	
Interest Revenue		2.609	370.317
Outflows			
TAB Cost of Sales	72.320		
Wagering Tax	40.417		
Wagering Services Expenses	82.549	195.286	
Racing Services Expenses	15.557		
Support Services Expenses	29.996	45.553	
Grants and Subsidies		2.199	
Distributions			
• Racing	113.662		
• Sport	4.003	117.665	360.703
Net Profit after Distributions			9.302

Ultimately the level of net profit will be determined by the distributions paid in the year. The 2009/10 year saw the combination of the Global Financial Crisis, the onset of the equine influenza impact on racing in the Eastern States, and Tabcorp pooling charge increases all work to result in a reduction in distributions by RWWA because of diminished profitability. This immediately led to reduced levels of racing stakes prizemoney, particularly in thoroughbred racing, reflecting the fragile nature generally of the funding models of animal racing. The WA Racing Industry is finely balanced and leveraged to the wagering based income distributions and other funding flowing from the wagering placed on its product. This will be discussed in detail in Chapter 5 of this Report.

RWWA has accordingly adopted a very constructive and prudent risk management approach to this situation of building up cash reserves to provide a cash buffer capability to smooth out any potential volatility in its profitability from wagering performance or general industry changes. RWWA's 2013 Annual Report reflected a cash and cash equivalent balance of $67.7 million, with a net working capital position of $32.2 million, which suggests a cash reserve buffer of around possibly $40 million for these purposes.

The $5 million of special distributions to Racing Clubs provided at the end of the 2013/14 financial year indicates an enhanced profit performance by RWWA for the year, and it is understood that further money was able to be put aside for these cash reserves balances.

Overall RWWA reflects a very solid financial position with good annual performance, cash reserves, it owns its property and computer system assets, and is debt free. The questions to be examined later in this Report revolve around the sustainability of RWWA's wagering profitability, what position the racing industry of Western Australia is in flowing from these distributions at present, and coming out of these is the issue of the sustainability of the Western Australian racing industry.

3.2 Privatisation

3.2.1 What is Privatisation?

Privatisation is the process of transferring ownership of a business, enterprise, public service or public property from the public sector (a government) to the private sector, either to a business that operates for a profit or to a not-for-profit organisation. It may also mean government outsourcing of services or functions to private firms.

The Western Australian Government has not yet reached the stage of defining exactly what it is seeking to privatise when it refers to the potential sale of the WATAB. However, it would seem reasonable to assume that it is referring to looking to transfer RWWA's wagering responsibilities to a non-government owned entity. A number of RWWA's functions that involve integrity, compliance and administrative oversight of racing and of wagering activities generally would logically not be activities that would be traditionally or logically privatised. Accordingly, throughout this report it will be assumed that it is just the wagering activities of RWWA undertaken under the TAB and TABtouch brands that are being considered for privatisation, which will be called WATAB. In effect this means that these activities would be separated out from RWWA for the purposes of sale.

The remaining activities and functions of RWWA will obviously still need to be performed (potentially by Racing Western Australia (RWA)-RWWA without the first W for wagering), which will be discussed in more detail later in the Report.

3.2.2 Forms of Privatisation

The actual transfer of ownership of a business or an activity from a government owned entity to a private operator (privatisation) can in fact occur in many different forms, with very many aspects within each of these forms that can significantly impact the attractiveness, value, and impacts on stakeholders of such a privatisation. In general terms privatisations can occur by:

1. **Share Issue Privatisation** – under this method the Government forms a company into which it transfers the wagering operations and then floats the company on the stock exchange by selling shares in the Company to private investors. The Victorian (1994), New South Wales (1997) and Queensland (1999) TAB's were privatised in this way.
2. **Asset Sale Privatisation –** selling an entire organisation (or part of it) to a strategic private investor, usually by an auction process or through direct negotiation with a natural buyer. Privatisations of this type have occurred with the TAB's of Northern Territory, South Australia, Tasmania and most recently the Australian Capital Territory, as well as most lottery operations around Australia.

   Such a sale can be achieved through selling the shares of a company that the Government has put the wagering operations in, or it can simply be selling the actual wagering operations assets without the whole company being sold. Whilst these two alternatives effectively end up with a similar operational outcome, they can be very different in legal terms for the buyer.

   The potential privatisation of WATAB will be discussed in detail in Chapter 6 of this Report. However, the key element in a TAB privatisation is the licence to operate the TAB's wagering business. If a TAB wagering business is sold without a licence, but a new licence is issued once the business operations have been purchased, it is possible that the ACCC's jurisdiction in the matter is quite different than if the business is sold with an existing licence.

3.2.3 Privatisation of WATAB

Given what has been discussed above, the Report now will consider what may be involved in a privatisation of WATAB, and how it might occur.

Firstly, given a number of factors, particularly that WATAB does not have its own betting pools and hence relies on others for pooling and/or betting management, and the increasingly competitive and somewhat cluttered wagering operator space in Australia, it is unlikely that the Government would consider trying to sell the WATAB thorough selling shares on the stock exchange. All three TAB's privatised in this manner had their own betting pools of significant size, in a time of no corporate bookmakers and supporting interstate betting arrangements that provided the basis for such an approach. This is not the case today nor for WATAB's operations.

These factors do also significantly impact upon an asset sale to a strategic investor, but are matters that can be managed by a buyer who has existing, broader and complementary interests that enable the buyer to deal with the risks differently than an existing stand-alone WATAB floated on the stock exchange would present.

If an asset sale privatisation was to be undertaken of the WATAB how might it therefore proceed. The first step would be to separate the WATAB operations from the rest of RWWA, identifying the specific assets, people and operations that apply to the running of the WATAB. The assets and operations that would be transferred, sold or newly instituted in any potential privatisation would likely include:

- The wagering IT system, including the central wagering software and equipment and terminals, including self-service terminals
- The website and mobile application software that underpins the electronic / on-line betting of WATAB
- The pooling agreement with Tabcorp
- The fixed odds management agreement with William Hill
- The licencing and agency agreements with all the retail TAB outlets
- All the account customer details
- Any specific intellectual property in wagering products, systems and branding/ marketing
- Employment contracts with all relevant staff
- Potentially the head office property (although what remains of RWWA may retain this property)
- Premium customer relationship arrangements
- The authority that currently exists under the RWWA Act to be the exclusive provider of retail wagering betting in Western Australia
- Arrangements with Western Australia racing clubs and authorities to provide on-course wagering services
- The various government funding and reimbursement arrangements in place under the various pieces of legislation and regulation within which WATAB operate.

The additional fundamental questions that will significantly impact the attractiveness and therefore the value of the WATAB business will be whether the wagering tax regime and the Distributions and all other funding to the WA Racing Industry currently faced by RWWA as part of its wagering functions remain in place at the current levels or at all. In addition, whether all the items outlined above as assets are to be part of the sale, and what value a prospective buyer may place on each of them, will also affect the attractiveness and value of the business being privatised/sold. These are all discussed in Chapter 6.

3.2.4 Structures of Australian TAB Privatisations

Whilst this Report will deal specifically with racing industry funding models in Chapter 6, this section sets out the actual structures involving the 3 key parties to TAB privatisations – the Government, the privatised TAB and the Racing Industry – that have evolved from each States' TAB privatisations.

New South Wales:

- On privatisation in 1998, TAB Limited, now Tabcorp, received a 99 year wagering licence with 15 years of retail exclusivity, and the NSW Racing Industry and TAB Limited entered into a 99 year contract, known as the Racing Distribution Agreement (RDA).
- The RDA governs the number of race meetings, fees due to the racing industry, and governance arrangements.
- TAB Limited pays distributions to the Racing Industry as follows:
  - 21.64% of net revenue
  - 25% of net profit
  - An annual lump sum of $12 million (CPI indexed|)
- Given the net profit component within this agreement, the arrangement operates as a form of partnership.
- Licence for retail wagering exclusivity extended to 2033 in 2013 for payment of $75 million.

South Australia:

- TAB Queensland, now Tatts Group Ltd, acquired the SATAB in 2001 with an exclusive licence to 2100, with all bets through SATAB going into the Tatts wagering pool.
- SATAB is therefore a branch office serving its retail distribution channel.
- The SA Racing Industry receives funding from SATAB of 42% of gross wagering revenue and the SATAB paid 6% of gross wagering revenue in wagering tax to the South Australian Government.
- The wagering tax on racing was removed in 2012 to provide improved racing industry funding, having been phased down from 2009.

Victoria:

- Upon listing the Victorian TAB under the name of Tabcorp, Tabcorp obtained a wagering licence and an electronic gaming machine licence running to 2012 and was required as a condition of the licence to enter into a 75%/25% joint venture arrangement with the Racing Industry.
- A new licence commenced in August 2012 for 12 years with the following financial agreement :

Victorian Wagering and Betting Licence and Tabcorp Wagering's arrangements with the Victorian racing industry (from August 2012)	
Joint Venture (JV) profit share	• 50% Tabcorp • 50% Victorian racing industry
Sole retail wagering and betting licence under the Gambling Regulation Act 2003 (Vic)	• Sole licence authorising wagering and betting on approved betting competitions via a Victorian retail network
Tax rates under the Gambling Regulation Act 2003 (Vic) (incl. GST)	• Pari-mutuel (thoroughbred, harness and greyhound racing): 16.69% of revenue • Fixed odds: 13.47% of revenue • Simulated racing events (Trackside): 20.00% of revenue
Product fees	• Product fee of 15.0% of pari-mutuel, all fixed odds and simulated racing events (eg Trackside) revenue and betting exchange commissions
Program fee	• $72.6m, subject to indexation
Race fields	• JV will bear race fields fees on non-Victorian product.
Asset Charge revenue	• Tabcorp's net recovery is 50% of depreciation and financing costs given its 50% interest in the JV
Victorian Racing industry benefit	• Victorian racing industry to receive 11.51% of pari-mutuel revenue on thoroughbred, harness and greyhound racing, which is to be paid by the JV. The rate may change with reference to state tax rates that may apply
Minimum performance obligation	• Minimum aggregate amounts to be received by the Victorian racing industry, with Tabcorp Wagering to pay any shortfall o $337 million in FY2013; o $342 million in FY2014; o A total of $1 billion (including the amounts set out above) in respect of the period from licence commencement to the end of FY2015 • These minimum aggregate amounts are subject to certain exceptions, (including in relation to retail exclusivity)

Queensland:

- When the Queensland TAB privatised via a float on the Australian Stock Exchange under the name TAB Queensland (now Tatts Group), Racing Queensland Limited (RQL) entered into a Product and Program Agreement with Tatts under which RQL provides Tatts with access to both Queensland and national racing programs in return for a fee of 39% of race wagering revenue.
- Tatts has a race wagering licence until 2098 with retail exclusivity up to 2014.
- Tatts and the Queensland Government recently renegotiated the licence terms as follows:
  - Race and sport wagering licences both run to 2098, with retail exclusivity to 2044.
  - Wagering tax on pari-mutuel reduced from 20% to 14% of margin, and fixed odds from 20% to 10% of gross margin

    Variable product fee of 39% of gross wagering revenue with ability to offset national and international racefield fees against the variable product fee (but with certain shortfall provisions if offset exceeds RQL's racefield receipts), plus $15 million fixed product fee (CPI indexed), and 2.5% of retail fixed odds sports revenue capped at $5 million per annum (indexed).
  - Licence fee of $150 million paid in instalments to the Government over 10 years
  - Other marketing, joint venture and exclusive on-course advertising commitments.

Tasmania:

- Tatts Group Ltd acquired the Tasmania TAB (Tote Tasmania) in 2012 for $103 million
- The arrangements put in place for Tote Tasmania post the sale is that Tatts pay an annual licence fee of around $7.0 million (CPI escalating) with no wagering tax and no product fees payable to the Tasmania Racing Industry
- Tasracing, a state owned company representing all three codes in the Tasmanian racing industry, is funded by the Tasmanian Government through appropriations worth $27 million a year over a 20 year period, and indexed annually over the life of the 20 year funding deed.
- Tatts Group has a retail totalisator licence that runs for 50 years, with a further 49 year option. The licence is exclusive for 15 years.

Northern Territory:

- TAB Queensland, now Tatts Group purchased the NTTAB in 2000 and with the sale was granted a Totalisator licence for a period of 15 years.
- Under the licence NTTAB pays 40% of gross margin on most events.
- The Department of Sport, Recreation and Racing manages the NT Government's industry funding agreements that are negotiated with the thoroughbred and greyhound racing clubs.

Australian Capital Territory

- Tabcorp purchased ACTTAB in July this year for $105.5 million
- The licences it has acquired is a guaranteed exclusive totalisator licence for 50 years, a sportsbetting licence for 15 years with further rolling extensions to 50 years, and ongoing approvals to offer Keno and Trackside products for 50 years.
- A licence fee on the totalisator licence of $1 million per annum (CPI indexed) is payable, but no wagering tax or product fees to ACT Racing entities are payable (similar to Tasmania). The wagering tax on the sportsbetting licence is expected to be less than 1% of turnover.

- The Government has entered into a funding arrangement with the ACT Racing Industry believed to represent around $8 million per annum to 2017, after which arrangements are uncertain but appear to possibly rely on a combination of on-course totalisator proceeds and some Government funding.

So as can be seen from the above there are various models by which TAB's have been privatised in Australia, which arguably have evolved from the variety of reasons for, and objectives of, Governments selling their TABs to privately-owned operators.

It needs to be recognised that the original privatisations of a number of these TAB's occurred under a completely different Australian wagering environment, specifically without corporate bookmakers and with the "Gentlemen's Agreement" operating (ie an informal agreement between TAB operators that they would each fund their own racing industry and allow other TAB's to offer wagering on their product on the understanding that no TAB would seek to sell bets into another jurisdiction). Accordingly, the models described above reflect a mix of the original structures and elements of updated arrangements given the passage of time.

In this context it is therefore extremely difficult to make any substantive judgements in relation to the success or otherwise of these privatisations, particularly as they relate to the respective racing industries, given the many intersecting factors that can effect a racing industry. It is important to understand that gambling in Australia is actually an activity governed under State/Territory powers – it is not under Federal Government jurisdiction.

So the Federal Government (other than through its telecommunication powers relating to transmission of data) cannot legislate in relation to gambling, it is a State/Territory power. Accordingly, the TAB's were State or Territory based and "owned", and racing industries evolved on a State/Territory basis. It has been through the corporate activity (through acquisition and/or pooling) of Tabcorp and Tatts that TABs have therefore been able to be combined and get some scale that State or Territory based TAB's were unable to achieve alone. Accordingly, in an overall sense, the privatisation of TAB's has provided a better scale and hence economics (in most cases) of TAB wagering operations for the various racing industries.

This has not however necessarily been the case for some specific State or Territory racing industries. Lack of local scale, and in the case of Tasmania some concerns on the TAB's operations, led to sale processes that saw the Government take over industry funding to achieve sales value, not a position recommended for the WA Racing Industry. The privatisation of South Australia TAB and perceived subsequent concerns with it could probably be associated with racing industry issues and some incomplete risk management structuring of the privatisation more so than the act of privatisation itself. With Queensland there is often a reference to flat distributions following privatisation, which would appear to flow from the wagering challenges faced in the performance of the TAB and a period of some flux in the local racing industry. NSW and Victoria reflect scale and scope in their wagering operations and their racing industries that could be said to flow from privatisation of the TAB (but it is difficult to be specific).

The following section explores some of the reasons why Governments may elect to privatise their government-owned TAB.

3.2.5 Why Privatise a TAB ?

There are a number of reasons why a State Government may choose to seek to privatise its TAB, and these include:

1. To reduce government debt levels that are causing high interest expense to the annual budget, and/or to address concerns around the credit rating of the State.
2. The Government determines that it should no longer be associated with the ownership of gambling operations.
3. The Government is of the view that as a result of wagering industry structural change, of industry competition, and/or of the general outlook for wagering turnover, that value is to be maximised by a sale at this time.
4. The Government is of the view that passing the operations to a privately-owned operator is a better model (financially and perhaps politically) than government ownership.

Of the reasons above 1, 3 and 4 largely run to financial matters and to questions of value in relation to the consideration of whether through the act of privatising the TAB the State receives better value than if it retains the TAB in government ownership. The second reason is often raised as a convenient social policy argument to justify a sale that is effectively an economically justified one (particularly for the first reason outlined above), particularly in the situation where other gambling assets are government-owned, such as a lottery business. This position must not, however, by confused with an argument that such privatisation of ownership is inconsistent with allowing other forms of gambling, eg Casino operations. Correctly regulating and taxing gambling operations and requiring licence fees/payments is different from ownership and should not be seen as inconsistent with a Government looking to sell a gambling asset it currently owns.

In any discussion as to the matter of value for a privatisation as outlined above, the fundamental decision for the State Government is whether the value the State receives from the sale of the TAB to private owners outweighs the value the State receives from ongoing government ownership of the TAB.

This value equation will have both financial and social considerations, and will include impacts upon the following:

Direct Financial Benefits

- The wagering tax inflows to the Government from the TAB
- The product (racefield) fees received by the State from interstate and international wagering operations wagering on Western Australian product
- The Distributions, the costs of racing operations and integrity services, and other payments paid to racing clubs and participants in the industry by the TAB from Western Australian and interstate/international punters turnover

- Profitability after WA Racing Industry funding by WATAB/RWWA
- The investment by owners and other participants into the local racing industry
- Flow on economic effects to and from the many suppliers to the industry, and to all local businesses from raceday events

Social Benefits

- Community benefits (even to the extent of meeting Community Service Obligations) of racing, particularly regional racing, to local cities and towns
- Employment
- Assistance to charities from racing activities

These are clearly all the factors that the State Government needs to weigh up in both its decision of whether to privatise or not, and if it chooses to, what should be the structure and operational framework. In its simplest form, the amount that a potential buyer will pay for a TAB is largely dependent upon:

a. What the buyer believes is the amount of net margin revenue it will generate through that TAB.

b. What it will cost to generate that margin in operating cost terms

c. What wagering taxes it needs to pay

d. Whether and/or what amount of product fees (or distributions) and other funding it needs to pay to the racing industry.

Accordingly, the Government will significantly impact the value (and hence upfront sale price it achieves) by decisions in each of these areas, with examples of issues pertinent to each corresponding particular area outlined above being:

a. Whether the buyer can expand the gambling product range, and whether existing unclaimed dividend and fraction provisions apply to the benefit of the buyer. Also critical is the length of the wagering licence/authority provided, and the exclusivity timings attached to it.

b. Whether the buyer is required to maintain existing employment and agency distribution arrangements, and/or for how long?

c. Does the wagering tax base and /or rate change under a privatised model?

d. Does the racing industry funding obligation stay with the wagering authority/licence and hence the buyer is required to pay a product fee, and, if so, what level of commitment is part of the sale?

These will be explored in detail in Chapter 6 where we discuss the implications of privatisation of the WATAB to the Western Australian Racing Industry.

4.1 Introduction

This section of this Report will provide some background on the wagering industry in Australia, the position of pari-mutuel (Totalisator) betting within the wagering industry, the landscape of TAB's and other wagering operators, and the position of WATAB/RWWA within the Australian wagering industry. As outlined in the previous section on privatisation, in any discussion on selling a government-owned TAB it is necessary that consideration be given to the position, performance and outlook for the entity itself in this case, WATAB/RWWA, as well as the wagering industry more generally.

4.2 Wagering Industry Participants

The major participants in the Australian race wagering industry are:

- The punters – the people who place bets on racing, sports and other events with the wagering operators
- The wagering operators – the organisations that provide the pari-mutuel and fixed odds wagering product, including WATAB/RWWA
- The racing industry – the racing clubs and associations, racing industry administrators, the breeders, the owners, the trainers, the jockeys/drivers, and all their industry employees, who provide the racing product and the events at which the product is displayed on which the wagering occurs and for which the industry receives product fees, racefield fees, various other forms of funding, and in some cases a proportion of the wagering operators earnings.
- Media broadcasters – the media companies who provide the vision of the races through various arrangements to the punters via broadcasting rights obtained from the racing industry on which the racing industry receives rights fees.

The focus in this section will be on the wagering operators and WATAB/RWWA's position within this group.

4.3 Wagering Operators in Australia

Wagering operators that provide betting services within Australia can be classified into the following groups:

- On-course bookmakers
- Corporate bookmakers
- TAB's
- Other wagering operators

These are explained below.

4.3.1 On-Course Bookmakers

On-Course bookmakers are licenced to provide fixed odds betting in each state and territory at the racing venues within that state or territory (although regulations have changed in recent times to provide more flexibility to these bookmakers in terms of telephone and on-line wagers).

4.3.2 Corporate Bookmakers

Corporate bookmakers are licenced off-course bookmakers who typically operate via telephone and internet/mobile applications. As the name suggest they are incorporated public/private companies that have typically been licenced and, in a technical sense operate from, the Northern Territory (NT) providing racing and sports betting, and in some cases betting options on other events.

The Northern Territory approved Australia's first sports bookmaker, Centrebet, in December 1992, and Centrebet became Australia's first on-line sports bookmaker in 1996. Today there are a number of corporate bookmakers licenced in the Northern Territory. The attraction of being licenced in the Northern Territory are the much lower wagering duties and taxes, low licencing fees, and much more flexible operating requirements than other States, with 24/7 capability.

The main corporate bookmakers operating in Australia are:

- Bet 365 - licenced in NT and owned by Bet 365 in the United Kingdom
- Betchoice/Unibet – formally Betchoice, Unibet (Swedish public company) acquired the business and its NT licence
- Betezy/BetEasy-BetEasy is the new brand after Betzy, licenced in the NT, was acquired by Sportsbet co-founder Matthew Tripp.
- Betfair – betting exchange licence in Tasmania and now wholly owned by Crown Resorts
- BetFred – licenced in the NT but not significantly active
- Ladbrokes – Owned by Ladbrokes PLC, Ladbrokes Australia acquired Gaming Investments which operated Bookmakers.com.au and it, together with Ladbrokes.com.au, have Norfolk Island licences. Recently acquired NT licenced Betstar
- Luxbet – licenced in the NT and owned by Tabcorp.
- NT Tab – licenced as a corporate bookmaker and TAB in the NT and owned by Tatts Group
- Paddy Power – Irish based UK listed company ownership that acquired Sportsbet and IASBet, both licenced in NT
- William Hill – owned by UK listed William Hill PLC and owns Sportingbet Australia, Centrebet and Tom Waterhouse licences in NT

Given the potential economic model for corporate bookmakers offered by the low cost structure, and arguably more flexible and lighter regulatory environment provided by the Northern Territory Government, locally owned corporate bookmakers began to commence operations under these Northern Territory licences. In fact, other than the Betfair licence in Tasmania, those listed above all operate on Northern Territory licences.

In many cases these locally owned corporate bookmakers would have operations (at least a server and relevant operatives) in NT as well as operations in their home State, with all betting going through the NT licence. The objective appeared in many cases to be to grow market share based on wagering turnover and to create a large customer database as quickly as possible, without profitability necessarily being a priority. This would provide the opportunity to establish a business of sufficient scale and customer penetration that could be attractive for potential larger corporate wagering operators either domestically or from offshore.

This opportunity arose also from the existing TAB's not having developed quickly or sufficiently enough their fixed odds offering nor their internet based system technology presentation, given their continued growth and profitable largely retail and telephone based pari-mutuel wagering business. The Corporate Bookmaking businesses attacked this opportunity by taking advantage of their low cost licences to provide more attractive odds and to adopt large marketing budgets as the means to seek significant customer acquisition for their account based customer lists.

Their low cost licences also enabled these corporate bookmakers to offer a product called Best Tote Odds under which the bookmakers effectively acted as resellers of TAB odds (sometimes with an added amount to the dividend given their cost advantage), with offset back into the tote pool if they wished, and hence benefit from their cost structure at little to no risk. These corporate bookmakers used the TAB's price IP at no cost, establishing a product of interest to punters. This has been a major source of growth for a number of these corporate bookmakers.

As account customer numbers and turnover growth, rather than profitability, seemed to be the major business objective, many of these operators ran their businesses at low margins to offer attractive odds, at times arguably not economically rationally from a wagering sustainability viewpoint. Nevertheless they were growing turnover and customer lists, and together with product and system innovation, were growing the Australian wagering market, and taking market share from the TAB's.

The successful High Court proceedings brought by Betfair Pty. Ltd, against the Western Australian Government in 2008 (Betfair Pty. Ltd. V Western Australian Government) removed concerns about potential advertising and market access limitations for Corporate bookmakers. Whilst the economic model for these bookmakers was however detrimentally impacted by the imposition of Racefield Fees through State Governments' legislation through 2008 and 2009 (with some subsequent court cases), these developments brought some clarity to the operating and financial models of these businesses.

With this, together with the related changes to the Australian wagering landscape, international wagering operators (particularly out of Europe) who were looking for expansion opportunities, identified Australia as an area for investment. Accordingly, as outlined above in the current list of Corporate Bookmakers, these international companies have largely acquired the local businesses, pushing up margins given the need for profitable growth on their shareholders' invested funds, and bringing their international capabilities, particularly in sportsbetting and technology, to these businesses. Section 4.4 provides some numeric perspectives on their impact on the Australian wagering market.

4.3.3 TAB's (Totalisator Agency Boards)

TAB's (Totalisator Agency Boards) or Totes as they are often called, were established in each State and Territory of Australia between 1961 and 1985, primarily to provide a legal race wagering vehicle and to facilitate the racing industry receiving funding from race wagering which was using its product. This was to remove all betting with what were in most jurisdictions illegal SP bookmakers who were not paying the industry for the use of its product. The TAB's were set up by Government legislation under Government ownership and given authority/licence to operate pari-mutuel betting exclusively for off-course retail, and for on-course in certain jurisdictions and included the obligation for the TAB's to fund the local racing industry given the provision of this exclusivity. This pari-mutuel exclusivity has been extended to telephone and internet/on-line services, and TAB's also now have fixed odds authorities/licences that are non-exclusive.

As outlined in Section 3.2.4 on privatisation, all Australian TAB's except the WATAB have since been privatised in one form or another, and there has been significant consolidation within the TAB's over the last 20 years. So as of today there are effectively three TAB groups operating throughout Australia (although each State and Territory still has its own TAB, given the State based gaming legislation, but owned and operated within one of the Groups). These three are:

- Tabcorp Holding Limited (Tabcorp)
- Tatts Group Limited (Tatts)
- WATAB/RWWA

4.3.3.1 **Tabcorp**

Tabcorp Holdings Limited is listed on the Australian Stock Exchange with its head office in Melbourne. Tabcorp operates businesses in Wagering, Media (Sky Channel), Keno and Gaming Services (TGS). Tabcorp's wagering business is comprised of the TAB licences in Victoria and NSW, and this year it acquired the ACTTAB, and also owns and operates the Luxbet corporate bookmaking business licenced in the Northern Territory. Tabcorp also operates at selected TAB's a simulated racing event game that is called Trackside.

At present Tabcorp is not permitted to combine its NSW and Victorian pools and accordingly operates them separately as the NSW pool and the SuperTAB pool out of Victoria. ACTTAB pools into SuperTAB, as does WATAB/RWWA.

4.3.3.2 **Tatts Group**

Tatts Group Limited is listed on the Australian Stock Exchange with its head office in Brisbane. Tatts Group operates businesses in Wagering, Lotteries and Gaming systems. Tatts Group's wagering business is comprised of the TAB operations in Queensland, South Australia, Northern Territory and Tasmania, and the corporate bookmaking licence held by NTTAB in the Northern Territory. Tatts Group operates one pool combining all of its operations for each of its pari-mutuel and fixed odds betting products and events respectively (ie there is no pooling).

4.3.3.3 **WATAB/RWWA**

WATAB's details as the sole remaining government owned TAB has been discussed in Chapter 3 of this Report.

4.3.4 Other Wagering Operators

Other wagering operators that offer punters the ability to bet on Australian product are betting exchanges and overseas bookmakers.

- Betting Exchanges: acting like many proposition warehousing business, such as a stock exchange, punters are able to offer prices for betting propositions and other punters can effectively deal directly with that punter through the betting exchange. The exchange operator takes a "clip of the ticket" when a transaction is done. Betfair is the only currently operating betting exchange licenced in Australia, and operates fully on-line. It has a licence in Tasmania and is wholly owned now by Crown Resorts.
- Overseas bookmakers: bookmakers based overseas and not licenced in Australia can offer wagering to Australian residents. Whilst the legalities of this activity are not entirely clear, such operators do not pay racefield fees to the Australian racing industry, depriving the Australian industry of some revenue, with the potential to offer better prices to punters because of this.

4.4 Sizing the Australian and Western Australian Wagering Markets

4.4.1 The Australian Wagering Market

Based on figures from the Australian Racing Board Fact Book 2013 the total turnover of the Australian Wagering Market for that year was around $24.5 billion (excluding Betfair and Trackside turnover). These figures include total turnover on thoroughbreds, harness and greyhounds racing and sportsbetting. The break-up of this $24.5 billion (which includes all TAB and bookmaker betting) is as follows :

Code	**$billion**	**% of total**
Thoroughbred	14.462	59.01
Greyhound	3.738	15.25
Harness	2.316	9.45
Sport	3.991	16.29
Total	**24.507**	**100.00**

Of this total wagering turnover, in the 2012/13 year, almost 2/3 of the turnover (66%) was via TAB's and around 1/3 (34%) with bookmakers. This split has changed from around 71.6% for TAB's and 28.4% for bookmakers in 2009/10.

Features of the Australian wagering industry that underlie this trend in the market (as also derived from figures obtained from the Australian Racing Board Fact Book) are as follows :

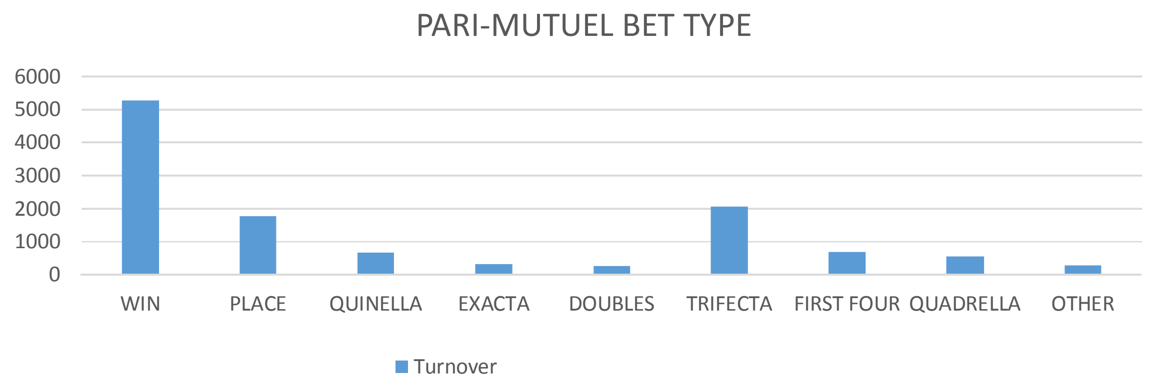
- Effectively all the growth in the wagering market over that period has been achieved by the corporate bookmakers, with total TAB wagering at around the same level in 2012/13 as in 2009/10.
- Sportsbetting as a percentage of total wagering turnover has increased from around 13% in 2009/10 to almost 16.3% in 2012/13 exhibiting growth of 35.5% over that time (a 10.5% compound annual growth rate), and continues to grow at a rapid pace (having grown at a compound annual growth rate of 12.8% in the last 10 years).

- This reduction in share of total wagering turnover for racing has been reflected by relatively flat thoroughbred and harness levels over that period, with greyhound betting increasing by over 27% during the same period.
- Retail TAB turnover has reduced by almost 16.5% between 2009/10 and 2012/13, whilst on-course TAB turnover has reduced by nearly 19% over the same period.
- For TAB's this retail pari-mutuel turnover decrease has been effectively replaced or transferred to fixed odds betting, which has more than doubled in TAB's over that time (with fixed odds on racing contributing over 90% of this growth).
- Fixed odds betting over the period from 2009/10 to 2012/13 has grown in total by almost 40%, and over the last 10 years has had a compound annual growth rate of 12.9% per annum, whereas pari-mutuel wagering has had a compound annual growth rate over the same period of -0.1%.
- In relation to total TAB betting, total pari-mutuel betting's proportionate share has declined from 87% in 2009/10 to 73.7% in 2012/13. This represented a fall from 61.6% to 48.7% of total wagering turnover over the period (this is based on all TAB sportsbetting being fixed odds – which whilst not correct is not materially inaccurate given the relatively low pari-mutuel sportsbetting that occurs). Pari-mutuel betting showed substantial declines in 2012 and 2013.
- On-line betting with both TAB's and particularly bookmakers has grown significantly, with bookmakers on-line betting alone increasing by over 76% from 2009/10 to 2012/13.

These observations clearly reflect the recent trends in the Australian wagering market. The growth of the phone and on-line based corporate bookmakers has been a major feature, powering the increased growth in fixed odds betting as a proportion of total Australian wagering turnover. As outlined earlier in Section 4.3 on Wagering Operators, these corporate bookmakers have benefitted from the low tax and fee structures of the Northern Territory to competitively price and heavily market their offer to the punters of Australia.

The corporate bookmakers have contributed substantially to the overall wagering turnover growth in Australia, bringing broad product offers, new on-line offers and technology design and functionality, and significant marketing and advertising to the industry.

As stated above, this growth of the corporate bookmaker has been a big driver of the increased popularity of fixed odds that has also driven growth of fixed odds in the TAB's. As clearly this is a product that is applied particularly to the most popular betting propositions of win and place betting (see the chart below for all Codes pari-mutuel betting types from page 67 of the Australian Racing Fact Book 2012/13), this had led to the shift away from pari-mutuel betting within TAB's as observed earlier, as it is a direct substitute product.



From a racing industry point of view the implications of these developments in the Australian wagering industry landscape are extremely significant given the importance of wagering to the funding of the racing industry. The growth of corporate bookmakers is arguably at the expense of TAB growth (although it can be legitimately questioned whether the TABs with their exclusive retail arrangement would have necessarily otherwise have fuelled the growth that has occurred). Whilst the TAB's, as explained earlier, have and/or had established product fee arrangements to fund the racing industry at substantial levels, no such arrangements applied to corporate bookmakers licenced in the NT. Accordingly, these corporate bookmakers were utilising racing product from all States and Territories with no obligation or requirement to pay the racing industry anywhere for this product.

State and Territory Governments in Australia addressed this (in part) through introducing Racefields Fees legislation to apply in their respective jurisdiction giving the relevant Government the power to require wagering operators who use any racing product information from their State or Territory for wagering purposes to pay a product fee to the Government and/or the Principal Racing Authority (PRA) in their State or Territory. In addition, the wagering operator can only legally use this information with the approval of the relevant PRA. Accordingly, all wagering operators are now required to seek approval and then pay these product (or racefield) fees monthly to each respective State based on specific rates and bases established within each jurisdiction.

As outlined earlier, in Western Australia this occurs pursuant to the provisions of the Racing Bets Levy Act 2009 and its associated Regulations, with the levy monies paid to the Gaming and Wagering Commission under Section 14A of the Betting Control Act, and then paid to RWWA (after deduction of expenses) by the Commission for distribution to Racing Clubs under Section 110B of the RWWA Act.

These Racefield or Product Fee Arrangements are set out in Table 4.4.1A.

Table 4.4.1A - PRODUCT FEE RATES 2014/15

State	Code	Rate 2013/14	2014/15 THRESHOLD	RATE 2014/15
NSW	Thoroughbred	1.5% Turnover 2% premium race meetings listed in schedule	Turnover under $5 million – 1% fee and t/o applied to standard meetings first	1.5% S and 2% P – Rates will increase following legislative change to remove cap – all codes
	Harness	1.5% Turnover 2% premium on meetings that have at least one race with prize money of $30k or more	Nil	Capped 1.5% Turnover standard meetings and 2% t/o premium meetings
	Greyhound	15% of Gross Margin with maximum fee capped at 1.5% of Turnover	Nil	Capped 1.5% Turnover standard meetings and 2% t/o premium meetings
VIC	Thoroughbred	1.5% Turnover 2% premium race meetings listed in schedule	Turnover under $5.5 Million = 1%	Pari-mutuel 1.5% t/0 Std, 2% t/o Group and 2.5% t/o Premium FOB – Greater of 1.5% or 15% GR Std 2% or 20% GR Group 3% or 30% GR GRP 1
	Harness	2.0% Turnover		1% payable on assessable t/o up to $100,000 on pari and FOB per calendar month and 2% payable on assessable t/o exceeding $100,000 on pari per calendar month 2.5% payable on assessable t/o exceeding $100,000 on FOB per calendar month
	Greyhound	1.5% Turnover	Turnover under 250k per month which equates to $3m per year = Zero fee	1.5 Turnover on Pari-mutuel 2% Turnover on FOB

QLD	All Codes	1.5% Turnover 2% premium month May – June	Turnover under $5 million = 1.5% • Premium=T=$75k,H=$25k, G=$10k • Other non-tote = Derivative and exchange betting	Pari-mutuel Standard t/o – 1.5% Pari-mutuel Premium t/o – 2% FOB Standard t/o – 2% FOB Premium t/o – 1.5% All other Non-Totalisator Bets Standard t/o – 2.5% All other Non-Totalisator Bets Premium t/o – 3.5%
SA	All Codes	13% GM 18% GM April 1 to May 14 (6 weeks premium weeks thoroughbreds only)	1% first %83k for thoroughbred t/o only (ie $1m @ 1% then normal rates)	**Thoroughbred** Std = 15%GR for first $10m / month then 10%GR Group & Listed Prem = 20% GR **Harness** Std = 15% GR January Prem = 18% GR **Greyhounds** Std = 15% GR 11 Sept – 10 Oct Prem = 18% GR
TAS	All Codes	If the net turnover of relevant approval holder exceeds $83,333 during the payment period, an amount that is greater of (i) 0.5% of that Net turnover and (ii) the aggregate of: 13% of Net Revenue 15% on Thoroughbred races during Jan and Feb Less if that Net revenue exceeds $850,000 during the payment period, 3% of that Net Revenue exceeding $850,000 in the Payment Period or if the Net turnover of the Relevant Approval Holder does not exceed $83,333 during the Payment Period, nil. All amounts inclusive of GST.		

ACT	All Codes	1.5% Turnover	Nil	1.5% Turnover and 2% on Black Opal race meeting
WA	All Codes	1.5% Turnover 2.0% for thoroughbreds only in November and December (premium rate) 1.0%for annual turnover below $2.5 million. If generate under $1,000 in any month then no fee levy payable in that month.	Turnover under $3.0 million – 1% fee on all turnover up to this amount. If generate under $1,000 in any month then no fee levy payable in that month.	Differential levy rates, which only apply once the threshold is reached, are: • Pari-mutuel bets place on standard race meetings levied at 1.5% of turnover. • Pari-mutuel bets placed on premium race meetings levied at 2.5% of turnover. • Betting exchange bets placed on standard race meetings levied at 1.5% turnover • Betting exchange bets placed on premium race meetings levied at 2.5% turnover • Non betting exchange fixed odds bets placed on standard race meetings levied at 2% of turnover • Non betting eschange fixed odds bets placed on premium race meetings levied at 3% of turnover A higher levy applies across all race codes and to any race meeting that is determined to be a premium race meeting. Premium race meetings are defined in the regulations on the basis of the value of stake money, as follows: • Thoroughbred racing - any meeting that contains at least one race with stake money of $100,000; • Harness racing - any meeting that contains at least one race with stake money of $50,000; • Greyhound racing - any meeting that contains at least one race with stake money of $30,000.

These Racefield Fees are at levels significantly below that which is paid by a TAB under it product fee structures with the local racing industry, particularly for pari-mutuel betting.

This brings us to the next issue of the growth of fixed odds, particularly through bookmakers. As fixed odds betting for the wagering operator is a much riskier business than pari-mutuel, and by definition therefore the margins may on average be lower and more volatile, the capacity to pay product fees is less than for a pari-mutuel TAB pool operator. The current levels that have been set as set out in Table 4.4.1A have been established by Governments on the basis of inputs from many parts of the wagering and racing industries and can be seen to be clearly substantially below the rates of which TAB's fund the racing industry. This is not in any way to suggest parity with TAB's given the retail exclusivity that TAB's enjoy, but the disparity between the two is considered too great and reflect a real risk to future funding for the racing industry.

The debate over these rates for racefield fees will continue, with an international benchmark of 3% currently a more comparable "royalty" rate with others around the world. However, for the racing industry, the continued growth of fixed odds betting in corporate bookmakers at the expense of TAB's (especially pari-mutuel betting) puts pressure on the future funding models of the racing industry. This situation is clearly exacerbated by the growth in sports betting for which the racing industry has no right to product fees if such betting is perceived to come at the expense of racing wagering by punters.

These issues, and many others underlying the trends in Australian wagering markets discussed earlier in this section, and which will impact the future outlook for wagering in Australia, are outlined in the following table developed by Mr. Sacha Krien, the Australian-based gaming sector analyst at CLSA Asia – Pacific Markets in Sydney – Table 4.4.1B. Sacha has not only listed these issues but also provided his views on where potential benefit or risk lies for the major TAB's and for Corporate Bookmakers. It provides an interesting insight into the future outlook facing WATAB/RWWA as a stand-alone TAB.

CHART 4.4.1B - TOP 24 WAGERING ISSUES

	Issue	Tabcorp	Tatts	Corporate Bookmakers	CLSA view
1	Market growth over time – HDI less 1%	✓	✓	✓	Base case: household disposable income (HDI) growth1% on higher turnover offset by falling win rates. We expect wagering to hold its share of overall gambling spend
2	In play betting – Will it grow the market	✓✗	✓✗	✓	Minor positive to Tabcorp/Tatts, but more upside for online-only operators
3	Can retail wagering grow from here?	✗	✗	-	We expect retail to fall to 30% of turnover by FY20 (versus 42% in FY12); equates to a 0.5% contraction pa
4	Which retail business will outperform?	✗	✓	-	Tatts has been slower to adopt new initiatives, but planned rollout of SSBTs should see it outperform Tabcorp (ex-trackside)
5	Once online, what share for Tabcorp and Tatts?	✗	✓	✓✓	Tabcorp's scale could drive further share gains short term, but declines in the medium term. Tatts can grow via new apps and by targeting NSW/Vic
6	Tatts' online expansion into NSW and Victoria	✗	✓✓	✗	Cross-selling to lottery database should see growth in Tatts' markets and at attractive margins given TasTote licence
7	Exotics the final frontier	✓✗	✓✗	✓	Totes have advantage, but competition from corporate bookmakers will increase with scale
8	Innovation and wagering	✓✓	✗	✓	Arguably Tabcorp is the market leader, but not for in-play betting
9	Bookmakers' price advantage	✗	✗	✓✓	Lower fees and taxes mean bookmakers can offer better odds than Tabcorp/Tatts or direct more resources towards advertising
10	Tote-odds betting	✗	✗	✓	An easy win for bookmakers and unlikely to be stopped any time soon.
11	Tote versus fixed-odds racing	✓✗	✗	✗	Contrary to popular belief, the margin upside for Tabcorp is insignificant unless fixed win rates stay above 12%. The threshold is higher for Tatts
12	Multibets – Sometimes size matters	✓✓	✓	✗	Tabcorp and Tatts have some competitive advantage here, offering more legs and bigger payouts: should drive improving sports win rates
13	Race-field fees – Turnover versus gross-profit tax	✓	✓✓	✗✗	Turnover taxes are here to stay
14	Race-field fees – Why they may go up over time	✗	✗	✗✗	Race fields' fees are the only means by which racing can target bookmakers for funding. Tabcorp is caught in the crossfire
15	Racefield fees – Impact of an increase	✗	✗	✗✗	A race to the bottom: a smaller revenue pie but a larger share to racing industry (paid for by bookmakers and Tabcorp)
16	Sports product fees	✗	✗	✗	We believe these are going up and will continue to rise over time
17	Win-rate sustainability	✓✗	✓✗	✓	The offshore experience suggests retail win rates are sustainable, but internet win rates will be squeezed
18	Rise of sports over racing	✓✗	✗	✓✗	Sports growth should outstrip racing – good for Tabcorp's margins but share of this product is less, plus it increases risk of higher industry product fees (race-field fees)
19	Free Wi-Fi but with access restrictions	✓	✓	✗	Minor positive if rolled out across Tabcorp and Tatts' retail network
20	Retail exclusivity – The next challenge	✓✗	✓✗	-	Exclusivity risk overstated for Tabcorp in NSW and Tatts in Qld
21	Premium punters and back-betting	✓	✓	-	Rebates could come down after the sale of TasTote – a positive for Tabcorp and Tatts
22	Future of broadcast rights In racing	✓✗	-	-	We expect a deal with TVN but at a cost - possibly an additional A$10m pa
23	Tote pooling	✓	✗	-	International tote pooling (the joining of tote pools from different jurisdictions) is not well understood. Could be a material boost for Tabcorp earnings. Conversely, without international pooling, Tatts' pools coud become more volatile
24	Industry consideration	✓✗	✗	✓	Consolidation among bookmakers creates stronger rivals for Tabcorp and Tatts. Merging Tabcorp with Tatts makes sense, but unlikely near term

4.4.2 WATAB/RWWA and the Western Australian Wagering Market

With the backdrop of the previous section's discussion of the Australian wagering market generally, this section specifically looks at WATAB/RWWA's wagering performance and trends within the Western Australian market specifically. In a headline sense, total TAB wagering growth from 2008/09 to 2012/13 in WA was 28%, compared to a national figure of 5%. Total wagering growth in WA was 22.6% over that period (clearly driven by the TAB wagering growth) compared to the national figure of 11.7% (predominantly grown by corporate bookmaker fixed odds growth).

When these TAB growth figures are broken up between pari-mutuel and fixed odds (but for a period of 2009/10 to 2012/13 given the availability of figures from the Australian Racing Facts Book), Total Australian TAB wagering pari-mutuel betting has declined by 14.3% and fixed odds has grown by around 105%. The comparable figures for Western Australia are 25.2% growth for pari-mutuel and 40% for fixed odds. In considering these figures it is also important to understand that in relation to TAB figures, in 2012/13 nationally the pari-mutuel / fixed odds share was around 73.8% / 26.2%, whilst the split for WATAB was 95.7% / 4.3%, a dramatically different position. (It is understood that in 2013/14 WATAB's fixed odds has grown substantially and changed this mix significantly).

As information is not available from corporate bookmakers as to the locations of their customers it is not possible to ascertain the extent of Western Australian punter wagering that is being directed out of the State to corporate bookmakers.

The relatively lower growth in WATAB's fixed odds betting than the national TAB figure may suggest either that:

- Fixed odds betting appetite is being directed predominantly to corporate bookmakers, or
- Fixed odds betting penetration is low generally in Western Australia for both the WATAB and corporate bookmakers.

Whilst more anecdotal than having any strong factual base, it would be suggested that the answer probably falls more with the latter (but with a contribution from the former perspective) given the lack of advertising and receptiveness to sponsorship by WA Racing Clubs in respect of corporate bookmakers.

From discussions with RWWA management, market research would appear to reinforce this view, in that Western Australian punters do appear to be quite parochial to the local provider by a significant amount. Until recently this has manifest itself in good pari-mutuel growth given the poor pricing, marketing, and delivery of the fixed odd product by WATAB/RWWA in the past. It is understood from RWWA Management that WATAB/RWWA's fixed odd turnover has grown substantially in the last year, which would appear to have arisen from more recent improvements in a number of aspects of fixed odds product delivery. These improvements include:

- Better and expanded pricing through improved operation of the fixed odds book
- Side-by-side provision of pari-mutuel and fixed odds pricing on retail displays and on digital channels, and improved racewall positioning
- Expanded product coverage, both domestically for harness and greyhound racing and nationally for all Australian racing
- The Soccer World Cup is a major fixed odds customer acquisition and volume enhancement event.

WATAB/RWWA is obviously significantly lagging other TAB's and Corporate Bookmakers in this regard, but is starting to show strong growth off a low base which should continue for a handful of years as it catches up with national trends. It is instructive to note, however, that the previously referenced market research does show increased, albeit not large, increases in awareness and usage of corporate bookmakers by WA punters, which is a threat to the extent and length of improved local TAB fixed odds wagering growth.

The higher growth in WATAB's pari-mutuel betting has resulted in the trends identified nationally of declining thoroughbred and harness racing pari-mutuel betting not being replicated in Western Australia to the same extent, and with stronger growth in pari-mutuel greyhound racing than the national growth. This would largely appear however to have resulted from a significant growth in premium punters (from within and outside Western Australia) attracted by rebates being offered by WATAB to these punters as an entry point into Tabcorp's SuperTAB pool.

This was a development that occurred within the Tasmanian TAB in the years before its privatisation, but at significantly greater levels than is believed is currently occurring in WATAB. It is believed that Tabcorp could be wanting to limit this, particularly given the Tasmanian experience.

Whilst premium punters have the ability to bring significant volume and liquidity to the pool, they tend to be more successful and hence win at greater rates than the bulk of local punters. Given the set prize dividend payout ratio for pari-mutuel betting this means that these premium punters can therefore reduce the effective prize returns ratio (and hence prize dividends) for the rest of the pool participants. These impacts obviously are not as profound in larger pools with greater liquidity, such as the SuperTAB pool into which WATAB/RWWA pools. Effective management of the pool is therefore represented by managing the trade-off between the volume and liquidity introduced by premium punters against the potential distortion for other pool participants by controlling the size of the premium punter contribution into the pool.

It is believed that this increase in premium punters has predominantly, but not solely, contributed to WATAB/RWWA's pari-mutuel turnover growth. It should be noted here that this solid wagering turnover and returns performance of WATAB/RWWA can also be attributed to a number of other factors, in addition to the growth of premium punters, including:

- The introduction of a new betting system, Phoenix, and associated new terminals – a system acknowledged as a good retail and premium punters wagering system
- Improved pooling services and management contracts with Tabcorp and William Hill respectively, both in terms of product spread and of financial arrangements.
- Improved fixed odds take up, on both racing and sportsbetting, due to product expansion and enhanced retail/digital information displays
- Improved liquidity and pricing across its product suite flowing from these enhancements.

In relation to Western Australia generally, it should also be observed that local bookmaking turnover effectively halved between 2008/09 and 2012/13 and continues to decline quickly, with essentially no local bookmaking activity on harness, greyhound and sport, and declining thoroughbred local bookmaker betting as evidenced by Perth Racing stating that they are budgeting for no income in the 2014/15 year from bookmakers on-course. This has been accompanied by declining on-course totalisator turnover which has fallen overall in Western Australia by nearly 20% between 2009/10 to 2012/13, with Perth Racing stating in its case the reduction had been almost 50% in the last 5 years. The primary causes of this on-course tote decline appear to be falling attendances, limited to no fixed odd offer, the absence of call betting, and the impact of competition from corporate bookmakers.

RWWA management have advised that 2013/14 has seen continued growth in wagering turnover in WATAB, but with a significant drop in retail pari-mutuel wagering that was more than offset by an equally large increase in fixed odd racing betting and continued growth in premium customers.

In Section 4.4.1 on the national wagering market there is a table reflecting the break-up of total wagering turnover across the three racing codes and sport for 2012/13, which is repeated in the first column below. The second column reflects this split nationally if Northern Territory is excluded (given the corporate bookmaker impact there). The third column is the Western Australian break-up (including TAB and bookmakers).

	National	**National (Ex NT)**	**WA**
Thoroughbred	59.01%	62.18%	49.70%
Greyhound	15.25%	17.12%	28.51%
Harness	9.45%	10.64%	15.70%
Sports	16.29%	10.06%	6.09%

This reflects a relatively much lower proportion for sports betting in Western Australia, (reflecting the lower fixed odds penetration and lower inroads of corporate bookmakers) and the relatively larger proportions to harness and greyhounds relative to thoroughbreds when compared to national averages.

The TAB wagering turnover growth for each State and each Code within each State for the period 2006/07 to 2012/13 are reflected in the table below:

	WA	QLD	SA	NSW	VIC
Thoroughbred	19.0%	7.3%	-5.9%	4.14%	8.0%
Sport	144.4%	73.6%	106.8%	78.9%	197.5%
Harness and Greyhound	58.9%	5.2%	-8.6%	16.4%	14.7%
Total	39.1%	9.5%	-3.6%	13.9%	17.6%

Clearly over this period WATAB/RWWA has been the most successful of the larger TABs in the country in relation to turnover growth. It is estimated that this growth figure for WATAB of 39.1% would reduce to somewhere just above 18% if premium customers were excluded from the figures – this is still above the growth rates of TAB's in these other States.

In acknowledging the good performance of WATAB/RWWA over this period, it is important to also position this in the context of previous performance of WATAB when it was a separate entity prior to RWWA's formation. Prior to the TAB being absorbed into RWWA it operated as a standalone business for which its relatively smaller size (when compared to Victoria, Queensland and New South Wales) and its limited product range (wagering product only) put it at a significant disadvantage compared to other TAB's. This reflected in a relatively higher proportionate cost base, and with less capacity to more proactively respond to advances in technology. These matters were all raised in the Turner Report. This needs to be considered in the context of the TAB in Western Australia not having electronic gaming machines in pubs and clubs to compete with as do other juristictions.

Accordingly, the performance of the WATAB/RWWA over the recent years has reflected to a large extent the catch up of what had been achieved in other TAB's in previous years. This is not a criticism of recent management, it is simply a statement of observation and perspective to enable readers to understand where WATAB/RWWA currently sits, and why at some stage in the future it will have caught up with the rest of the mature TAB's wagering operations in terms of product, technology, platforms and competition. Reflections of this specific point are illustrated by the following observations of previous growth trends and the more recent initiatives in relation to features previously reflected in other jurisdiction's operations:

— The comments on the delayed introduction of an effective and efficient fixed odds offer as explained earlier in this Section 4.4.2

— For the period from 1986/87 to 1993/94 WATAB grew its turnover by 71.4% against the Queensland TAB growth rate over the period of 104.5% per the Australian Gambling Statistics, 29th edition, as released by the Government Statistician of Queensland Treasury and Trade in February 2014

— Over the same period NSW TAB turnover grew by $1.4 billion, Victorian TAB turnover by almost $1.0 billion, and WATAB turnover by just $240 million

— The decision to enter into, and in more recent times more fully expand the pooling arrangements with Tabcorp to deal with the implications of its pools being small, so as to increase the liquidity and stability of prices for punters across essentially all products

— The recent addition of premium customers into the pool

— More recently improved retail information and betting systems, and investment in the digital platform

— The future rollout of greater numbers of self-service terminals (SST's)

— Just beginning the introduction of improved product offers and technologies for on-course totalisator operations.

This understanding of the positioning of WATAB/RWWA in the Australian wagering landscape is critical to any consideration of what is the best ownership structure for WATAB into the future.

This section seeks to establish a base line structural financial position for the Western Australian Racing Industry against which to then discuss the implications for the Industry of the potential privatisation of WATAB/RWWA.

In this context the WA Racing Industry is defined to include Thoroughbred, Harness, and Greyhound racing and encompasses all those employed in and/or those that participate in the production of racing animals and the production of the racing product. This Report will also discuss some of the suppliers to, and integral service providers to, the WA Racing Industry.

5.1 What is the Western Australian Racing Industry?

In accordance with the definition of the racing industry above, the Western Australian Racing Industry is therefore comprised of the following groups and their representation:

- **RWWA** – the Principal Racing Authority for each of the Codes, being the principal club for thoroughbred racing, the controlling body for harness racing, and the racing authority and registration authority for Greyhound racing. In accordance with the RWWA Act, to meet its requirement to consult with prescribed racing bodies, RWWA meets with each of the Codes through Consultative Groups established for each respective Code. Each Group has an established membership base consisting of RWWA officers and nominated representatives of various Code stakeholders.

- **Thoroughbred Code** – Perth Racing's Board has responsibility for the Belmont and Ascot racetracks. Western Australia's 9 Provincial Thoroughbred Clubs each have their own (voluntary) Boards and are members of the WA Provincial Thoroughbred Racing Association (WAPTRA).

  The Country Racing Association of WA (CRAWA) is comprised of the 25 Country/Community thoroughbred racing clubs around the State, all of which have their own (voluntary) Boards.

  Owners are represented by the WA Racing Owners Association (WAROA) and include a wide array of individuals. It is highly unlikely that any of these people are solely economically dependent on racehorse ownership for their livelihood, and many are breeders and trainers as well.

  Breeders have a representative group called Thoroughbred Breeders Western Australia (TBWA). Trainers have an association called the WA Racing Trainers Association (WARTA) that represents their interests. Jockeys interests are represented by the WA Jockeys Association (WAJA).

- **Harness Racing Code** – The Gloucester Park Harness Racing Club Board has responsibility for the operation of metropolitan harness racing at the Gloucester Park track. There are 7 provincial harness racing tracks that are operated by (voluntary) Boards. The WA Country Racing Association (WACRA) represents these provincial clubs as well as the 7 Country/Community Harness Racing Clubs that also have their own (voluntary) Boards.

  Owners of Harness Racing horses are represented by the Harness Racing Owners Association WA (HROAWA), as well as by BOTRA.

  Breeders of Standardbreds are represented by the WA Standardbred Breeders Association (WASBA), and also by BOTRA. Trainers and Reinspersons in Harness Racing are represented by BOTRA, the Western Australian Racing Breeders, Owners, Trainers and Reinpersons Association.

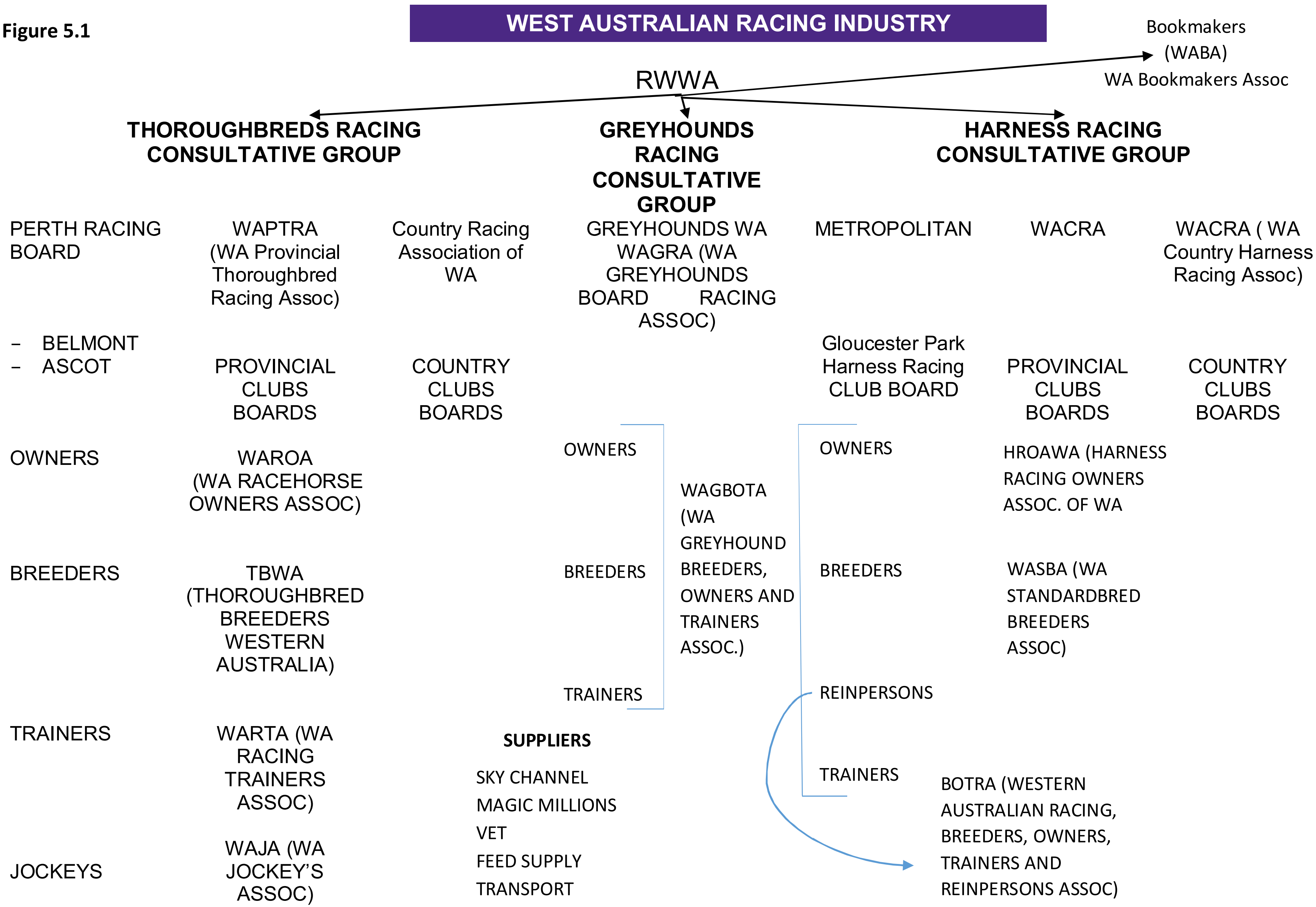
- **Greyhounds Code** – The Western Australian Greyhound Racing Association (WAGRA) is the designated greyhound racing club of Western Australia. It is established under the provisions of the Western Australia Greyhound Racing Association Act 1981 and is a body corporate. WAGRA is not a Crown agency, but the Committee of WAGRA is appointed by the Governor at the nomination of the Minister, and is subject to Ministerial direction. It oversees the operation of greyhound racing at Cannington, Mandurah and Northam in its role as a designated club under the direction of its Board/Committee.

  Owners, Breeders and Trainers of greyhounds are represented by the WA Greyhound Breeders, Owners and Trainers Association (WAGBOTA).

- **Service Providers** – There is a wide range of service providers to the Western Australian racing industry that rely on the industry to varying degrees, and the major areas of these include:
  - Sky Channel – vision of races
  - Magic Millions – arrange the annual yearlings sales in Western Australia
  - Veterinary services
  - Feed Supply
  - Transportation

These are all set out on in Figure 5.1 on the next page.

Figure 5.1


WEST AUSTRALIAN RACING INDUSTRY
RWWA
Bookmakers (WABA) WA Bookmakers Assoc
THOROUGHBREDS RACING CONSULTATIVE GROUP
GREYHOUNDS RACING CONSULTATIVE GROUP
HARNESS RACING CONSULTATIVE GROUP
PERTH RACING BOARD
– BELMONT
– ASCOT
OWNERS
BREEDERS
TRAINERS
JOCKEYS
WAPTRA (WA Provincial Thoroughbred Racing Assoc)
PROVINCIAL CLUBS BOARDS
WAROA (WA RACEHORSE OWNERS ASSOC)
TBWA (THOROUGHBRED BREEDERS WESTERN AUSTRALIA)
WARTA (WA RACING TRAINERS ASSOC)
WAJA (WA JOCKEY'S ASSOC)
Country Racing Association of WA
COUNTRY CLUBS BOARDS
SUPPLIERS
SKY CHANNEL
MAGIC MILLIONS
VET
FEED SUPPLY
TRANSPORT
GREYHOUNDS WA WAGRA (WA GREYHOUNDS BOARD RACING ASSOC)
OWNERS
BREEDERS
TRAINERS
WAGBOTA (WA GREYHOUND BREEDERS, OWNERS AND TRAINERS ASSOC.)
METROPOLITAN
Gloucester Park Harness Racing CLUB BOARD
OWNERS
BREEDERS
REINPERSONS
TRAINERS
WACRA
PROVINCIAL CLUBS BOARDS
HROAWA (HARNESS RACING OWNERS ASSOC. OF WA
WASBA (WA STANDARDBRED BREEDERS ASSOC)
BOTRA (WESTERN AUSTRALIAN RACING, BREEDERS, OWNERS, TRAINERS AND REINPERSONS ASSOC)
WACRA (WA Country Harness Racing Assoc)
COUNTRY CLUBS BOARDS

5.1.1 Sizing the Western Australian Racing Industry

Given this industry structure and governance/representation framework, this section provides a perspective on the size in terms of participants and economic impact of the Western Australian Racing Industry. In doing this it draws heavily upon the research report of IER Pty. Ltd., on the Size and Scope of the Western Australian Racing Industry undertaken for RWWA in 2012, entitled "Western Australian Racing Industry – Economic and Social Impact Report, September 2012" (the IER Report).

The IER Report was based on a study undertaken using 2010/11 financial year information, providing an extensive coverage of the economic and social contribution of the Western Australian Racing Industry to the Western Australian State and its economy. From examining a number of the key statistics of the WA Racing Industry as reported by RWWA annually in its publication "Industry Status Report', and specifically the 2013 report, a comparison of these key statistics (financial, race program and other racing statistics) reflects that a number of the 2012/13 financial year outcomes for key base measures for the WA Racing Industry are not materially different from those of 2010/11 on which the IER Report was based. Accordingly, in referencing outcomes of the IER Report, it is valid to assume that they remain largely reflective of the industry size today in general terms. This particularly applies to industry starters numbers, numbers of races, and the like – financial figures will have grown by specific rates of price inflation, wagering turnover growth, and general economic growth. The overview of the key data from this report is provided in Figure 5.1.1 on the following two pages which are pages 4 and 5 from the IER Report.

In this context the key statistics reflect that over the last couple of years the WA racing industry has essentially just maintained its position. From 2010/11 to 2012/13 the number of racing clubs has reduced by 3 to 53, the number of race meetings have increased by less than 1% to 880, the number of races has increased by 2% to 8,237, and the number of starters in races was essentially the same.

In this time the number of thoroughbreds and greyhounds that raced were the same, with only harness racing showing an increase. Disconcertingly, in relation to breeding, thoroughbreds born reduced by 17.5%, Standardbreds reduced by almost 30% and greyhounds reduced by nearly 4.5%. Of equal concern is that the statistics in relation to the number of registered persons in the WA Racing Industry also showed a declining trend (other than in thoroughbred jockey apprentices as a result of a specific strategic priority by RWWA in this regard). The number of registered thoroughbred trainers and jockeys are down, harness trainers and driver/trainers are down nearly 12% and 14% respectively, whilst the number of registered greyhound trainers are down by over 10% in the last couple of years.

This will be discussed later in this Report, but these trends reflect the fundamental position of the WA Racing Industry – distribution levels have been increasing to attempt to produce the racing product but the costs and risk/return profiles of the production of racing animals are not being met from these distributions leading to departures of participants and/or decreased yields/output as businesses and/or the number of individuals are cut back in size in an attempt to sustain involvement.

Overview of Key Data

Key Results at a Glance

Jobs & Participants (West Australians that rely in part or totality on the Racing Industry for their livelihood)	Total
Breeders	4,292
Trainers	1,692
Owners	16,745
Other Employees (i.e. stablehands, trackriders etc.)	4,327
Participants in the Production of Racing Animals	**27,058**
Raceclub & Industry Staff	3,250
Attendants, Stewards, Vets, Farriers	524
Jockeys & Drivers	166
Volunteers	753
Wagering Staff	1,935
Participants in the Production of the Racing Product	**6,628**
Total Employment & Participation	**33,686**

"One in every 54 Western Australian adult residents participate or are employed in the Western Australia Racing Industry"

"There is an average of more than two race meetings every day, providing entertainment and employment for Western Australian residents"

Racing	Total
Number of Racing Clubs	55
Number of Race Meetings	874
Number of TAB Races	850
Number of On-Course Attendances	868,166
Number of Racing Club Members	10,092
Value of Sponsorships	$4.9 mil

Nationally, consumption of harness and greyhound racing is higher (proportionally) in Western Australia than in any other State or Territory."

Racing Animals	Total
Number of Foals & Pups	2,643
Number of Animals in Training	10,214

"The production ($68.4 mil) and preparation ($113.9 mil) of racing animals is responsible for generating total expenditure of more than $180 million in Western Australia"

Wagering (WA TAB)	Total
Total Wagering Turnover Placed in WA	$1,764.0 mil
Net Wagering Revenue	$264.1 mil
Wagering Turnover (WA oncourse)	$82.3 mil
State Government Wagering Tax Revenue	$34.0 mil
GST Paid on Wagering Revenue	$24.5 mil

Source:- Australian Racing Fact Book & RWWA Annual Report 2010/11

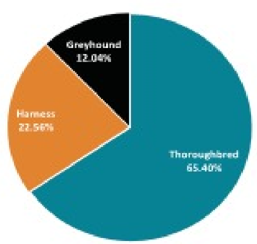
"The State Government receives more than $34 million from wagering taxes alone"

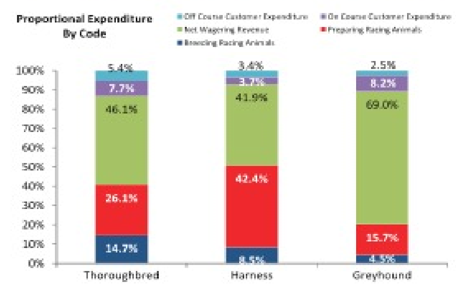
Overview of Key Data

Key Results at a Glance

WA Racing Industry Direct Expenditure	Total
Producing Racing Animals	$66.5 mil
Preparing Racing Animals	$157.2 mil
Net Wagering Revenue	$264.1 mil
On Course Customer Expenditure	$37.8 mil
Off Course Customer Expenditure	$25.3 mil
Total Direct Expenditure	**$550.9 mil**

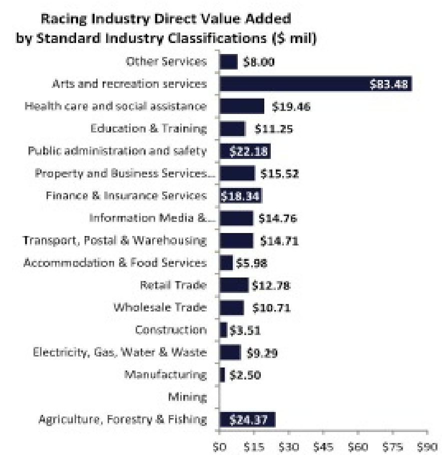
"The Western Australian Racing Industry generates more than $550.9 mil in direct expenditure. Nearly half of this expenditure occurs in regional areas"





"Racing contributes more than $594.6 million in value added to the Western Australian economy. The activities of the racing industry sustain the employment of more than 6,737

Economic Value of Racing in Western Australia	Total
Total Value Added Generated by Racing	$594.6 mil
Full Time Equivalent Employment	6,737
Household Income Generated	$349.3 mil



"In dollar terms, the racing industry generates its largest portion of expenditure in the Arts & Recreation sector, followed by Agriculture, Forestry & Fishing and Public Administration & Safety (Government)"

The IER Report establishes the broad economic impacts of the WA Racing Industry to Western Australia in the context of :

- Total employment and participation of over 33,000 people, reflecting "one in every 54 Western Australian adult residents participate or are employed in the Western Australian Racing Industry".
- "The Western Australian Racing Industry generates more than $550.9 million in direct expenditure. Nearly half of this expenditure occurs in regional areas".
- "Racing contributes more than $594.6 million in value added to the Western Australian economy". This represents around 0.14% of the State's total Gross Value Added.
- Full time equivalent (FTE) employment created/sustained by the WA Racing Industry is 6,730 FTE (including both direct and indirect impacts). The differential between participation and employment reflects the large number of part time and casual employees, the high amount of voluntary work undertaken, and the significant number of owners (almost 17,000).
- Estimated annual expenditure generated by racegoers of in excess of $56.4 million (excluding wagering), of which $31.2 million is direct and $25.3 million indirect (based on 81 cents being spent in the community for every $1 of expenditure made by an attendee at the races).
- The impact in the regional part of Western Australian from racing is around 50% of the total in terms of expenditure, and estimated at around 35% of the total level of activity contributed by racing.

5.1.2 Participants in the WA Racing Industry

As outlined above, the IER Report states that more than 33,000 people are directly involved in the racing industry in one way or another. These participants include paid employees, employers and volunteers (there are more than 750 volunteers estimated to be involved). These are set out in the table below taken from page 16 of the IER Report:

Participant Type	Thoroughbred	Harness	Greyhound	TOTAL
Breeders	2,633	1,560	99	4,292
Breeders Staff	2,614	972	33	3,619
Owners & Syndicate Owners	8,797	4,855	3,094	16,745
Trainers (Open Class/Trainer A/Public)	52	141	85	278
Trainers (B Class/Trainer B)	28	113		141
Trainers (Restricted Permit or Driver/Trainer)	595	433		1,028
Trainers (Owner/Trainer)	35		210	245
Trackriders/Stablehands	422	286		708
Participants in Producing Racing Animals	**15,175**	**8,362**	**3,521**	**27,058**
Full Time Club Staff	116	29	34	179
Part Time Club Staff	30	45	5	80
Casual/Contractor Club Staff	1,927	384	199	2,510
Club Volunteer	528	220	5	753
Jockeys, Drivers & Apprentices	104	62		166
Barrier Attendants/Handlers	237	29	79	345
Stewards	28	17	12	57
Farriers	31	31		62
Industry Vets	42	18		60
Participants in Producing the Racing Product	**3,043**	**835**	**334**	**4,212**
Industry Administration Staff				481
Totalisator Wagering Staff				1,935
Total Participants in the Racing Industry	**18,218**	**9,197**	**3,855**	**33,686 ***

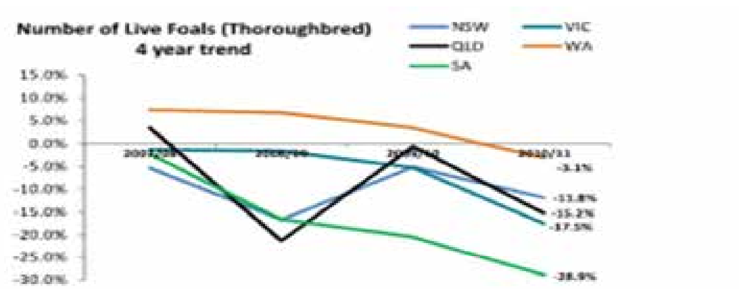
\# Cant be allocated to individual codes

Whilst many of these people rely on racing for their livelihood, the bulk do not as will be discussed later, and in fact many actually fund the industry through money, their time and their efforts to sustain the WA Racing Industry's operation. As IER states "Trainers, breeders, jockeys and drivers represent a segment of society whose investment in skills and infrastructure make them heavily reliant on a successful racing industry". It is equally evident from conducting this review that there are a large number of people employed by breeders and trainers particularly who as a result of their involvement in the WA racing industry have not prepared themselves for alternative employment and are equally dependent upon a sustainable racing industry.

Breeders

The breeding sector provides and replenishes the racing stock for the WA Racing Industry. The IER report stated that there are nearly 4,300 breeders in Western Australian, with over half of these in regional areas. Breeders range from large stud farms employing many staff and turn out large numbers of foals, to a large number of amateur and hobby breeders. The larger breeders are those primarily responsible within this group for the employment of around 3,700 staff in their operation. Breeders derive the majority of their income from the public and private sale of their stock.

In Thoroughbreds it is understood that there are probably 12 major commercial breeders of which half are standalone thoroughbred breeding operations and the rest are combined with other commercial interests. WA Thoroughbred breeding is impacted by the lack of depth in stallions, but the Westspeed bonus program is helping to partly offset the often too strong competition from Hunter Valley and Victorian large stud operations. There has been an overall declining trend in the breeding of thoroughbreds in Western Australia and nationally as reflected in the following chart from page 21 of the IER Report:



The other major feature of Western Australian breeding, which is common across Australia, is the need in many cases for breeders to take an ownership stake in a horse to get a sale done, such that it is estimated that around 68% of horses have a breeder holding a stake.

For harness racing, breeding is essentially a 4 year process, and the Westbred bonus system is critical to breeders by providing cash inflow relatively earlier in their total investment cycle. It is considered that around 90% of standardbred breeders are hobbyists, and it is understood that there are no big studs being standalone harness racing breeders. Only around 50% of horses bred actually race, reflecting the risk/return position here. Around 70% of breeders would own Standardbreds for the reasons identified above for thoroughbred breeders.

In greyhound breeding it appears that there are no standalone commercial breeders due to lack of returns to greyhound breeders. This Racing Code shows a great deal of breeding/training ownership integration to achieve an economic model, and again as with other Codes the WestChase bonus scheme has been important in supporting a level of local breeding, given however that the majority of greyhounds are now bred interstate and brought to Western Australia to race.

Trainers

There are around 1,700 horse and greyhound trainers providing services to owners in the WA racing industry. Training services generally incorporate the training (pre and race), trialling and raceday management of a racehorse or greyhound. Trainers employ and/or utilise the services of a variety of skilled and unskilled labour, particularly stable hands, farriers, track riders and vets to prepare racehorses and greyhounds. As the IER Report states for the more than 700 stablehands/track riders employed by trainers, for many the employment opportunity offered would otherwise be difficult to satisfy in the broader employment market. Nearly 58% of these jobs are sustained within regional areas of Western Australian.

Trainers' income is mostly generated through trainers fees charged to owners and a percentage of stakes prizemoney won.

There are various models and business sizes of thoroughbred trainers in Western Australia, and these differ also between metropolitan and regional given different stabling and training situations. Trainers are also significant part owners of thoroughbreds for various reasons – either through choice or need if their yearling purchases are not able to be fully on sold to external owners. With the absence of metropolitan stabling facilities many trainers own their properties through requirement, with this property in many cases representing their retirement/superannuation (although the ability to sell the property as a going concern is unlikely given the lack of cashflow economics across the racing industry). Staff employed by trainers operate under a federal wage award, although it would appear not all trainers necessarily comply with these requirements (probably due to the difficult economic model for trainers).

Harness racing training exhibits many similar attributes such as relatively low training fees causing a significant reliance on share of stakes prizemoney to survive, major stables having on track success that reduces returns to others to at or below sustainable levels, significant investment in property because it is required for stabling and training of horses (held as superannuation but depends on industry sustainability), and significant horse ownership by trainers.

Most greyhound trainers don't get paid a training fee – they agree to go into an equal ownership share of the greyhound. Again there are a variety of different models with some large trainers, but the bulk are small hobby trainers.

Current Major Considerations for Breeders and Trainers

In discussions with various representatives of these groups, there are a myriad of issues facing the sustainability of the WA racing industry, but at present two major considerations are:

(i) Lack of Confidence flowing from lack of clarity in the future of the Industry – this is primarily being impacted by two matters, the uncertainty over the implications of the potential privatisation of the WATAB/RWWA, and the confusion and uncertainty associated with major infrastructure of the WA Racing Industry, particularly Belmont, Ascot, Gloucester Park and Cannington.

(ii) The difficulty of isolation of the WA racing industry compared to the Eastern State Racing Industries who have the ability and mobility capacity to travel readily to other jurisdictions to get some diversity of circumstances if any of a wide range of factors are negatively impacting on the participant's local racing product performance. It could be argued that such isolation could be seen as a benefit as the WA racing industry more readily calibrates to the set number of racing animals and jockeys, although the import of greyhounds from the Eastern States for example might refute this.

Of course, the second of these is a simple reality but it becomes more significant when overlaid by the first point. Investment in the WA Racing Industry is and will continue to be constrained whilst there is significant uncertainty on these matters. Clearly both the WA Racing Industry and the WA Government have significant roles to play in providing some clear direction here within a relatively short timeframe before participants no longer see the benefit of continued investment in the WA Racing Industry.

Ownership

The following is from page 29 of the IER Report:

> "Owners provide much of the capital outlay and day to day funding for the production of racehorses and greyhounds. In 2010/11 there were more than 16,700 individuals with an ownership interest in the Western Australian Racing Industry.
>
> Considerable research over many years has shown that many owners do not consider their involvement to be a financial investment from which they require a return on investment. This is not to say however that owners are prepared to continue to fund their investment if there is diminished opportunities to realise a return".

This is reflected by separate analysis outlined in this Report to provide an estimation of the percentage return against funds invested (ie, total gross dollar returns expressed as a percentage of the total dollars spent) by owners in each Code in Western Australia which suggested the following ratios:

	Returns as % of Costs
WA Thoroughbreds	24%
WA Harness	34%
WA Greyhounds	36-50%*

*Based on 50/50 owner/trainer split

The IER Report cited that the large majority of owners in Western Australia (84.4%) are involved through an ownership syndicate. Whilst perhaps introducing more owners into the industry initially at its introduction, the recent change to now name up to 20 owners rather than only 10 in the racebook has resulted in owners now investing smaller amounts to achieve one of their desired objectives from ownership. This would not seem to have translated into more owners, just broadly the same amount of owners but with smaller overall investment.

Racing Clubs

Racing Clubs provide the venue and racing administration for the conduct of race meetings to allow owners to race their horses and greyhounds. As indicated earlier, there has been minor changes in the number of clubs, race meetings and races over the last couple of years, but as will be reflected later, there is very little if any margin in the operations of these Racing Clubs with them all dependent upon the RWWA distributions, subsidies and other funding for their viability. They are required to distribute 100% of their stakes distribution from RWWA as prizemoney.

Perth Racing, Gloucester Park Harness Racing Club and WAGRA have a number of full-time staff, provincial thoroughbred and harness racing clubs have limited staff, whilst country clubs have no full-time staff with Committee members (all volunteers) finding the task of their inputs increasingly challenging with increased OSH, integrity and security requirements. These issues, to differing extents, are affecting all Racing Clubs. Whilst stewards are provided by RWWA to all race clubs, many provincial and most country clubs are required to bring in staff for race days (in some cases from Perth) who need to be paid because of the regulated requirements and standards to be met, including security.

Many of these Racing Clubs provide a community service for their members, with the main racing days also providing a local business event for the town and a major opportunity for local charities. The number of members of racing clubs is around 10,000 of which around 2/3rds are with regional clubs and 1/3 with metropolitan clubs.

5.2 Funding of the Western Australian Racing Industry

This section discusses the funding of the Western Australian Racing Industry in the context of the sources of the funds that finance its operation, and how this funding flows through the value chains of each of the Codes to the stakeholders within, and suppliers to, the Code to produce the product of racing.

5.2.1 Overview of Funding

The funding into the WA Racing Industry, which will be analysed in greater detail in the Code value chain analysis in Section 5.3, can be effectively summarised as:

(1) The payments received from the wagering industry for using the product of the Racing Industry – that is, paying for the racing product on which they wager and receive money from punters. The Racing Industry owns the intellectual and property rights to this racing product, and needs to be appropriately paid for providing that product to the TAB's and other wagering operators who use it to generate income for themselves.

(2) Owners Contribution – as outlined previously, with owners of racing animals on average effectively contributing approximately 76% of thoroughbred cost, 66% of harness racing cost, and 50-64% of greyhound costs, for the potential of some return and for personal enjoyment and entertainment of horse and greyhound ownership, they are a major source of funding for the Racing Industry.

(3) Voluntary Contribution – the many volunteers on Racing Club Committees and those who provide raceday services for no remuneration are a significant contributor to the production of the racing product.

(4) Financiers to Racing Industry Participants – given the position of the WA Racing Industry this will effectively involve those institutions who are prepared to fund investments in property by the larger breeders, trainers and owners, who as we will see later are in many cases just generating sufficient to operate annually with the property as their superannuation/retirement funding. The other form of financing to the WA Racing Industry is Magic Millions which provides attractively priced funding terms for horses sold at their sales for many industry participants.

(5) Governments – through various programs, all levels of government provide some funding for WA Racing Industry infrastructure to supplement the relatively low levels of funding that the industry is able to fund from operations.

(6) Other Sources – there are various other sources of some funding of the WA Racing Industry which include sponsors (primarily of Racing Club events), expenditure by patrons attending race meetings, and other income sources of Racing Clubs outside of WA Racing Industry participants.

In identifying these major sources of funding it is not to ignore the significant investments by many within the WA Racing Industry. However, this analysis is looking at those groups that provide externally sourced funding to the participants within the industry who invest time and infrastructure into producing the racing product. Breeders and trainers for example are invested but look to fund these ultimately from owners, stakes prizemoney, bonuses, and other WA Racing Industry funding.

5.2.2 Distributions from RWWA to the Racing Industry

The major source of funding to the Western Australian Racing Industry is the distributions paid by RWWA, which are funded by the wagering industry, and largely by the operations of the WATAB. Not only is this the major source of funding, but as it largely determines the stakes prizemoney that fundamentally determine the levels of all other activity in the racing industry process, it is the critical driver of the entire industry.

5.2.2.1 **The Basis for Distributions / Payments by the WATAB to the Racing Industry**

As touched on earlier in the Report, in the processes of creating RWWA as the principal racing authority for each of the Codes and the creation of, and subsequent transfer of, the WATAB into RWWA, the racing industry has agreed to these actions and the taking on and use of its racing product rights in return for the commitment of the payment of distributions to racing clubs as outlined in Section 3.1.3 of this Report. That is, in return for having the exclusive retail wagering rights in Western Australia, the TAB first and then RWWA took on the obligation to fund the WA Racing Industry pursuant to the licence / authority for this exclusive wagering capability.

To be very specific in this regard, the WA Racing Industry as defined as the Racing Clubs and all of its Participants, are the owners of the product and intellectual property rights associated with the production of racing through the three Codes. Accordingly, as an Industry the Racing Industry invests significant time, effort and money in the production of what is the Racing Product.

Prior to the establishment of TAB's in this country, these product rights were being used by SP bookmakers who used racing as the basis for their in most cases illegal bookmaking activities with no payment or compensation to the Racing Industry for the use of racing product. In establishing TAB's Governments acknowledged these intellectual and product property rights by requiring TAB's to make product fee payments to the Racing Industry (and separately and differently tax payments to the Government) for the use of these rights to operate their totalisator pools through exclusive licences to operate retail wagering within the relevant State. This was the case with the establishment of the Western Australian TAB.

With the establishment of RWWA in 2003 under the RWWA Act, RWWA became the Principal Racing Authority for each of the Codes. The intellectual and property rights of the WA Racing Industry were effectively licenced to RWWA at that time by the Racing Clubs and Participants, the consideration for the licencing of rights was the continuity of distributions/payments to the WA racing industry, through RWWA, for the use of these rights by the WATAB, and recognition by the WA Government of the obligations of the WATAB to fund the WA Racing Industry for the exclusive retail wagering authority it received. When the WATAB became part of RWWA this commitment and requirement was legislatively reflected in Section 50 of the RWWA Act which states:

"50 (i) …………… the functions of RWWA in relation to gambling include the following –

-

-

-

(c) to develop and implement a scheme for the distribution of net profits and to negotiate funding arrangements with individual racing club."

The current distributions framework and other funding by WATAB/RWWA in place between the Racing Clubs and RWWA therefore reflects the currently accepted position of the WA Racing Industry and WATAB/RWWA in relation to this requirement, and hence establish both the process and current quantum under the process for payment by the WATAB to the WA Racing Industry in respect of WATAB's use of the Racing Industry's intellectual and racing product property rights.

This is reinforced in the RWWA Act through the provisions of Section 105 to 107 relating to distributions of funds to racing clubs by RWWA. Section 105 clearly reflects the embodiment in legislation of the quantum and distribution processes in place in the WATAB immediately prior to its transfer to RWWA for a three year period. Section 106 then, appropriately, identifies that quantum and allocations of such distributions between Codes will change over time and empowers, within frameworks, RWWA to establish the most appropriate criteria for these distributions. This is reflected in the current distribution quantums and allocations by RWWA.

Accordingly, given the current structure of RWWA with the TAB operation incorporated into its operations, the processes of decision-making, criteria establishment and distribution and overall total WA Racing Industry funding determination sit within and are embedded in the operations of RWWA and its Board And given the above, these become the current baseline for any consideration of the privatisation of the WATAB and the payments required of the privatised WATAB to appropriately compensate the WA Racing Industry for the provision of its intellectual and racing product property rights.

Any change in process and/or redirection in this distribution regime could be argued as an action of technically breaching an inherent contractual arrangement between the TAB and WA Racing Industry through Government Legislation (which, in an indirect fashion could be argued, the Victorian Government has seen the consequences of recently in a judgment made in respect of its actions in relation to Tatts Group's Gaming Licence in Victoria).

Privatisation has previously seen elsewhere, and it will in Western Australia if the WATAB is privatised, the result being the externalising of this position and will require an explicit contractual arrangement between the WATAB and the WA Racing Industry to lock in the requirement for such payments, supported by appropriate legislative and licencing requirements.

5.2.2.2 **Determining Distributions and the Allocation**

As has been outlined previously, Section 106 of the RWWA Act establishes the basis on which distributions to the Racing Industry by WATAB/RWWA are to occur. Clearly the framework here is that the value of the intellectual and product property rights made available to the WATAB are reflected in its ability to generate net margin from the use of this product, particularly under its exclusive retail wagering authority, which under Section 106 is then, after meeting all costs, distributed to the WA Racing Industry. Accordingly, the level of distribution and total racing industry funding is determined in this way and by its very nature therefore ensures the continued and sustained provision of this level and quality of racing product from the WA Racing Industry. As reflected in Section 5.3 of this Report, it is this level of distribution and total racing industry funding that finely balances the inputs and outputs of the WA Racing Industry to drive this outcome.

In relation to the allocation and composition of these distributions and other funding between codes, between clubs, and with participants, there are a variety of considerations that are obviously taken into account in their determination by RWWA in Western Australia's case, and by the PRA's in all the States and Territories. Whilst clearly not being privy to the detailed elements of this with RWWA, from an overview of States and Territories including Western Australia the factors in these considerations are broadly similar although in different forms and extents between States and Territories, and as applied to RWWA appear to be:

- Event Fees (Club Funding) – to fund the general expenses incurred by the club in the preparation and conduct of the race day event associated with the race program.
- Owners Incentive Distributions
- Abandoned meeting subsidy payments to Clubs and Participants
- Payments for Riders and Drivers Fees and Australian Jockey Association funding
- Stakes money – prizemoney both Base and Feature Races
- Training Services
- On-course Bookmaker Fees
- Breeders and Owners Subsidy payments – payments made to Breeders and Owners under Westspeed, Westbred and Westchase programs for each Code respectively.

All of these payments are technically made to the Racing Clubs but for payments to industry participants these are actually made directly by RWWA to the participants on behalf of the Clubs.

In the determination of payments under each of these and other payment types and the allocations to Codes, participants, and Racing Clubs in each year some of the factors considered would appear to include:

- The calendar of racing allocated between the different codes and courses
- The incremental changes proposed to this calendar but with a desire not to result in a Racing Club running into deficit due to the inability to meet underlying fixed cost elements of their operation
- Maintaining general benchmarking levels in terms of relativities of stakes prizemoney levels across States, so changes in other States raise the need to look at local focuses with the stakes allocations in Western Australia.
- In general terms looking to attempt to optimise the wagering and entertainment outcomes from the delivery of the racing product
- Balancing up across the program the returns to owners given the slightly differing profiles of these across the Codes.

- Ensuring that breeders, owners and trainers particularly are provided with and the State generally achieves the black type/listed racing requirements to support the pedigree of the Western Australian Racing Industry within the Australian racing landscape.
- To support the participation level of all those in the WA Racing Industry, including drivers/jockey fees and the like and appropriate breeders bonuses
- To cater for relativities of cost between city and country, and the travel requirements of many participants and officials to provincial/country race tracks
- Acknowledging strategic and competitive advantage opportunities such as Interdominions in harness racing.
- Funding of training facilities to ensure availability and affordability with subsidised user pays structures.

These are just a list of a few of the many factors that RWWA would be expected to consider not just in the context of the level and allocations of distributions and other funding to the WA Racing Industry annually, but in relation to the welfare and operation of the WA Racing Industry generally. At present such decisions occur within RWWA itself funded by the inflows it receives from the operations of WATAB. In any potential privatisation the financial arrangements between a privatised WATAB and the WA Racing Industry must ensure that funding to the Industry is maintained to meet these required outcomes to underpin industry sustainability and ensure the continued racing product provision to wagering operators (including the privatised WATAB).

5.2.2.3 **Levels of Distributions Paid**

The outflow of these legal obligations and distribution allocation decisions by RWWA are reflected in the distributions that have been made by RWWA since 2004/5. These are set out in Table 5.2.2.3 over the page derived from RWWA's Annual Reports and its annual Racing Industry Status Reports.

TABLE 5.2.2.3 RWWA DISTRIBUTIONS TO RACING CODES ($M)

YEAR	DETAIL	THOROUGHBREDS	HARNESS	GREYHOUNDS	TOTAL
2004/5	Participant Distributions				
	• Stakes	33.326	13.783	5.149	52.258
	• Other	4.434	2.307	0.132	6.873
		37.760	16.090	5.281	59.131
	Club Distributions	-	2.912	3.587	6.499
	TOTAL	**37.760**	**19.002**	**8.868**	**65.630**
2005/6	Participant Distributions				
	• Stakes	40.461	16.976	6.586	64.023
	• Other	5.866	3.712	0.364	9.942
		46.327	20.688	6.950	73.965
	Club Distributions	1.509	3.157	3.365	8.031
	TOTAL	**47.836**	**23.845**	**10.315**	**81.996**
2006/7	Participant Distributions				
	• Stakes	44.714	18.449	7.556	70.719
	• Other	7.096	3.667	0.354	11.117
		51.810	22.116	7.910	81.836
	Club Distributions	1.078	3.306	3.390	7.774
	TOTAL	**52.888**	**25.422**	**11.300**	**89.610**

TABLE 5.2.2.3 (cont) RWWA DISTRIBUTIONS TO RACING CODES ($M)

YEAR	DETAIL	THOROUGHBREDS	HARNESS	GREYHOUNDS	TOTAL
2007/8	Participant Distributions				
	• Stakes	48.742	20.422	8.340	77.504
	• Other	8.318	3.846	0.466	12.630
		57.060	24.268	8.806	90.134
	Club Distributions	3.795	4.950	4.062	12.807
	TOTAL	**60.855**	**29.218**	**12.868**	**102.941**
2008/9	Participant Distributions				
	• Stakes	51.082	21.248	8.734	81.064
	• Other	9.836	4.142	0.517	14.495
		60.918	25.390	9.251	95.559
	Club Distributions	3.448	4.752	4.213	12.413
	TOTAL	**64.366**	**30.142**	**13.464**	**107.972**
2009/10	Participant Distributions				
	• Stakes	48.396	21.392	8.687	78.475
	• Other	7.248	2.701	0.489	10.438
		55.644	24.093	9.176	88.913
	Club Distributions	5.315	4.364	3.850	13.529
	TOTAL	**60.959**	**28.457**	**13.026**	**102.442**

TABLE 5.2.2.3 (cont) RWWA DISTRIBUTIONS TO RACING CODES ($M)

YEAR	DETAIL	THOROUGHBREDS	HARNESS	GREYHOUNDS	TOTAL
2010/11	Participant Distributions				
	• Stakes	48.105	21.136	8.464	77.705
	• Other	7.671	2.413	0.456	10.540
		55.776	23.549	8.920	88.245
	Club Distributions	6.681	4.470	3.983	15.134
	TOTAL	**62.457**	**28.019**	**12.903**	**103.379**
2011/12	Participant Distributions				
	• Stakes	49.538	22.744	8.837	81.119
	• Other	6.062	2.707	0.498	9.267
		55.600	25.451	9.335	90.386
	Club Distributions	10.828	4.633	4.292	19.753
	TOTAL	**66.428**	**30.084**	**13.627**	**110.139**
2012/13	Participant Distributions				
	• Stakes	50.362	22.235	890.871	82.468
	• Other	8.026	2.768	0.575	11.369
		58.388	25.003	10.446	93.837
	Club Distributions	10.629	4.762	4.434	19.825
	TOTAL	**69.017**	**29.765**	**14.880**	**113.662**

It should be noted in Table 5.2.2.3 that while the total distributions figures by Code and the overall totals are as reported in the RWWA Annual Reports, the table has used actual stakes paid (as opposed to stake distributions made to Racing Clubs) to better reflect actual returns to participants.

Accordingly, the figures for other participant distributions and Racing Club distributions will differ from reported figures as they incorporate adjustments for when actual stakes paid vary from stakes prizemoney distributed to the Clubs. So whilst the actual component figures of the total distributions made in the table do not technically exactly align to the year to year figures as reported, they do reflect a good picture of participant returns. The underlying premise here is that the Racing Clubs had sufficient funds available to meet the top-up requirement so RWWA limited its stakes distribution to force the Racing Clubs to use these funds for stakes prizemoney to Participants.

In this context this approach starkly illustrates the impact on returns to participants when total distributions were reduced in 2009/10 for the reasons outlined earlier in this Report. The reduction of around $5.5 million in total distributions (5.12% decrease on the 2008/9 distributions) resulted in a $6.65 million reduction in returns to participants, or close to a 7% decrease on the 2008/9 return levels (with the major part of this in the thoroughbred code).

In the 8 years covered by Table 5.2.2.3 it can be seen that distributions to the Racing Industry have grown by 73.18% (just over 7% p.a.), with Thoroughbred distributions growing 82.77%, Harness 56.64% and Greyhounds 67.79% (around 7.25% p.a., 5.8% p.a., 6.6% p.a. respectively). For the period from 2009/10 to 2012/13 these figures are 10.95% in total, and for the Codes 13.22%, 4.6% and 14.23% respectively. It is interesting to note that for the period from 2006/7 to 2012/13 these figures are 26.84%, 30%, 17.08% and 31.68%, whilst wagering turnover for WATAB for that period has grown by 29.1%. A couple of factors contributing to this lower rate of growth in distributions compared to WATAB's turnover growth is the reduction in the margin return on turnover (with the growth of some lower margin fixed odds product and of premium player turnover), proportionately greater growth in sports betting and hence sports related distributions, and a decrease in the proportion that distributions represent of the margin as other revenues and costs have in net terms resulted in a lesser percentage of the margin generated by wagering being available for distribution and total racing industry funding purposes.

It is understood that with the recent one-off payment by RWWA of $5 million in additional grant distributions just before the end of July to assist Racing Clubs to address their Occupational Safety and Health compliance obligations, total distributions for the 2013/14 financial year were $130.8 million (including grants)

In relation to the allocation of racing industry distributions between the 3 codes, there has been minor movements year-to-year based on various matters including different priorities, events within specific Codes, and changes in available funding, but in overall terms the allocation has moved as reflected below:

Percentage of Allocation of Distributions to Racing Codes

	2006/7	**2012/13**
Thoroughbred	59.0%	60.7%
Harness	28.4%	26.2%
Greyhound	12.6%	13.1%
TOTAL	**100%**	**100%**

The movements between these two dates, subject to relatively small annual fluctuations as discussed above, reflects an effective gradual trend in these movements throughout the 6 year period.

5.2.3 Racing Club Funding

Racing Clubs are the entities that provide the venue and arrange the event that facilitates the presentation of the racing industry product. In this event presentation there is a wide range of racing club offers provided ranging from racing clubs that conduct just one meeting per year, though provincial clubs that have around mid 20's numbers of meetings annually, up to Perth Racing with 90 meetings between Belmont and Ascot, Gloucester Park Harness Racing with 93 meetings, Cannington Greyhounds 103 meetings and Mandurah Greyhounds conducting 162 meetings per annum. Accordingly, the financial models for these clubs do vary widely but there is one fundamental message relatively consistent to most if not all of them, and that is that they at best break even financially in an operational cashflow sense with little to no funds available for infrastructure expenditure. This section discusses the financial position of WA racing clubs.

Given this spread of racing club size and operation, the financial position and reporting of these clubs is equally varied, with no consistency in the way their financial reports are produced. RWWA does not in any way formally consolidate the financial position of Racing Clubs, probably both reflecting this inconsistency and/or in a sense also enabling this inconsistency to occur. For this Report, the annual reports of all but 9 small racing clubs were able to be obtained for the 2012/13 financial year which represented nearly 99% of the total stakes distributions from RWWA provided in that year.

Subject to the inconsistent accounting treatments (particularly in many cases only having the availability of net bar and catering profits or net on-course totalisator returns), some of the observations of the financial operations of WA racing clubs for the 2012/13 year are as follows:

- Total income (subject to some netting) was in excess of $160 million
- Total expenses (again subject to some costs having been netted against revenue) was in the order of almost $165 million
- For the Racing Clubs included in the analysis this provided a combined operating deficit of approximately $3 million (which approximates the loss of Perth Racing if its one-off other income (predominately from land sales) is excluded)
- Excluding its one-off income items Perth Racing reported a $2.710 million loss, Gloucester Park Harness Racing reported a $0.386 million loss, and the WA Greyhound Racing Association reported at $0.384 million loss.

- Around 66.5% of the total income of racing clubs appears to come from RWWA distributions and other funding (of which around 63% is stakes distributions). This increases to almost 68% when Perth Racing, Gloucester Park and Greyhounds are excluded from the combination analysis.
- Excluding Perth Racing, Gloucester Park and Greyhounds the total profit outcome is a surplus of around $0.8 million which in general terms reflects minor surpluses in provincial thoroughbreds, very small surpluses to break even in country thoroughbreds, and mainly losses in harness racing clubs.
- Other income outside of RWWA distributions and other funding is comprised largely of bar and catering sales and on-course totalisator, with some sponsorship, function income, admissions and member subscriptions, training in certain instances, and other miscellaneous inflows make up the rest. As discussed in Section 4.4.2, on-course totalisator income has been decreasing in recent times.

These combined Racing Club financial figures reflect that there is no capacity to reduce funding to the WA Racing Industry without significantly damaging the financial position and hence potential sustainability of many of WA's racing clubs.

This current position has evolved largely from the distribution philosophies of RWWA and the reductions in on-course totalisator income. It also reflects the limited capacity for investment in facilities leading to stagnating or declining attendances as the overall event product provided by Racing Clubs struggles to compete with alternative leisure and entertainment offers, whilst also feeling the effects of the less buoyant Western Australian economic environment.

From discussions with RWWA Management it appears the distribution framework for Racing Clubs was previously more loosely based around percentages of on-course and off-course wagering turnover they contributed and the extent of external non-wagering turnover the course generated. From later last decade onwards, however, it appears that Racing Club distributions were largely flatlined as a strategic RWWA decision to increase distributions to participants, primarily through stakes funding enhancements, but also to other requirements such as the Australian Jockey's Association. There appears to have been at least a twofold focus with this, that is :

- To provide a more targeted strategy in terms of stakes, given the 2 television stations now covering racing, to maximise product by increased focuses on areas such as black type race availability, and the comparability of the race program to other States.
- To remove the simple but sub-optimal model for Racing Clubs of simply putting on more meetings to get more funding (irrespective of whether or not overall product and profitability benefitted) that flowed from this wagering revenue performance model.

So the brunt of the downward adjustment to distributions required in 2010 flowing from the disruptions of 2008/09 was felt by the Racing Clubs as participant funding remained the focus, combined with what could be described as a fairly blunt policy decision to straight line event fees to deal with a poorly set performance indicator on wagering turnover for Racing Club funding. This wagering turnover based approach did not focus nor necessarily reward Racing Clubs or their performance to broader industry product issues such as quality of animals, appropriate racing field sizes, and exposure and promotion and attendance-orientated race programming.

From discussions with both Country and Provincial racing club representatives, this worsened financial position for Clubs was reflected in a number of further issues facing their ongoing viability as follows:

1. Recently imposed OHS requirements has had significant cost and cash drain impacts on Racing Clubs, together with the increased and new responsibilities placed on voluntary Committees of the Clubs (increasing personal exposure leading to volunteers walking away).
2. Integrity and compliance requirements for racing and event management are more complex, expensive and in some cases constraining. People often need to be transported in and paid, eg; security, because required skills are not readily available (again especially in the country where there are no full time staff).
3. The significant cost of travel, especially to country meetings, given the issues raised above and the sheer size of the State.
4. The inability to fund infrastructure requirements and maintenance out of existing operational funding sources.
5. Horse numbers are a challenge for country thoroughbred and harness racing clubs because of hard tracks, the economics of racing is difficult, and the tyranny of distance (Kalgoorlie actually has its own stock of horses).

With all of these issues the viability of WA Racing Clubs does now appear to have been recognised by RWWA, with some initial responses helpful in attempting to get Racing Clubs through. At present, there does not appear to be any fundamental change in Racing Club funding philosophies, but RWWA have taken initiatives such as:

- RWWA staff providing financial advice and support in terms of assisting the Racing Clubs in their financial management activities.
- The provision of special distribution payments totalling $5 million by way of grants to Clubs in late July 2014 on a pro-rata basis “for use in addressing vitally important Occupational Safety and Health (OSH) issues at your club”, as outlined in letters to Racing Clubs from the RWWA Chairman, Jeff Ovens.
- Initiatives being considered focused at improving the on-course totalisator wagering offer (which will help those with reasonable wagering facilities).

Greyhounds, with its 3 tracks all operated by WA Greyhound Racing Association, also faces many of these issues. In addition with event fees not changing, its response has been to put on more meetings to remain viable. Clearly the major issue at present is Cannington, which is now being partly funded by RWWA, but more funding is needed to properly complete the project.

Under its current leadership, WAGRA understands that it needs to right size its administration but needs around $1.3 million to fund the redundancy cost to enable this right sizing to occur. Such an investment is recommended by RWWA with the people cost savings being used by WAGRA to fund both the full completion of the new Cannington facility and marketing expenditure, with distribution levels maintained. Other infrastructure is understood to be in reasonable condition, although ageing, and hence Greyhounds require the same positioning on this issue as the other Codes.

It also appears that in many cases Racing Clubs' finances are also being held up by additional support from RWWA through a variety of subsidy payments to cover various areas including:

- making the Product Fee payments of Clubs in respect of their on-course wagering.
- Paying the Sky Channel vision costs for the Clubs
- In some cases, and to varying degrees, costs of on-course wagering are absorbed and/or paid by RWWA
- The costs associated with the infrastructure and operation of broadcasting the Clubs' racing through Sky Channel.

This list is unlikely to be exhaustive of the subsidies and other funding support provided by RWWA in addition to the distributions made to Racing Clubs (and participants).

Clearly therefore all of this starkly reflects the fact that WA Racing Clubs, as with the rest of the WA Racing Industry, is operationally break even under the current settings of the industry. With no real growth in distributions to Clubs coming from RWWA out of the WATAB wagering business profits in recent times, and declining on-course totalisator proceeds, the Racing Clubs have no fat in their operations and require at least the same level of current distributions and subsidies from RWWA to continue to remain viable.

In reviewing the balance sheets of those Racing Clubs that were able to be obtained, there does not appear to be any material buffer in their balance sheets to provide any mitigant to this operational risk position. For example, of the 22 provincial and country thoroughbred racing clubs balance sheets examined, the average net working capital position across these was an approximately positive $108,000 - $109,000 which is insignificant when you consider that the average annual RWWA distribution to Racing Clubs in these categories is around $487,000 per Club, ie. a liquidity buffer of just over 20% of just one year's distribution. Of course this is an average and this position is obviously much worse in a number of Racing Clubs. For provincial and country harness racing clubs these respective figures are around $35,000 and $584,000, and hence only a 13% buffer on average.

As discussed elsewhere in this Report, this situation with Racing Club financing of an operational break-even position and no substantial reserves leaves no capacity for any funding of infrastructure investment from within the current racing industry funding model. This is particularly concerning when, from the Racing Club balance sheet reviews undertaken it is clear that many Club facilities are fully or close to fully depreciated, and from visual examination of facilities many of them are clearly in need of expenditure, but no substantial depreciation charges against income are occurring to provide funding for such expenditure.

Specifically in relation to the metropolitan Racing Clubs, the following comments are made:

- Perth Racing has publically stated that there are a number of issues with their business/financial model of such concern that they have retained Deloitte to advise them on this matter. It is not appropriate for this Report to deal with these matters other than to say that in relation to a number of the issues raised in this section, many have relevance to Perth Racing.
- Gloucester Park Harness Racing Club also faces many of the same issues, and in fact its net working capital surplus only represented less than 12% of its annual RWWA distribution.
- WAGRA was discussed above, and again reflects a number of the same issues.

5.2.4 Funding by Owners

There are a wide range of financial models under which WA Racing Industry horse and greyhound owners operate – from commercially orientated for profits models with a large number of animals and generally also operating in other parts of the industry value chain, to hobbyist owners who may hold a small fractional holding in one or a small number of animals through a syndicate of a number of owners. Clearly in such a situation it is not possible to generalise nor realistically attempt to deal with all potential ownership models. For the purposes of this Report the discussion in this regard will utilise a basis of establishing an average ownership concept for a particular horse or greyhound, and use this average returns and costs to owner concept to give some estimated quantification of the magnitude of funding provided to the racing industry, on average, on an annual basis by owners.

Such an analysis by its very nature will be only a very high level indicative estimate based around raw averages and very many assumptions. Given that in all aspects of the racing industry value chain the approaches, training methods and philosophies, ownership frameworks and animal management practices will vary significantly, not to mention the animal themselves, such a conceptual approach will clearly be only very indicative. Whilst costings (which are likely to be understated given dated pricing data used in the calculations) and assumptions will obviously vary significantly in practice, this approach will nevertheless provide a reasonable basis on which to illustrate a critical aspect of the funding and sustainability of the WA Racing Industry (even if the preciseness of the figures may be questioned). An outline of the assumptions and calculations for this analysis approach are set out in Appendix 1 to this Report entitled "Return to Owners – Code Cost to Race Ratios".

This analysis provides the following outcomes:

	Return to Owners Ratio
WA Thoroughbreds with Acquisition Costs	24%
without Acquisition Costs	38%
WA Harness Racer with Acquisition Costs	34%
without Acquisition Costs	38%
WA Greyhounds with Acquisition Costs at $5,000	50%
with Acquisition Costs at $10,000	36%
without Acquisition Costs	99%

Given these figures, the remainder of this section will therefore reference that WA Thoroughbred owners effectively fund 76% of the cost of racing a horse, harness owners fund 66%, and Greyhound owners fund 64%.

The returns to owners that therefore make up the balance of the costs of owning and racing the animal are funded by the major components of the distributions and other funding from WATAB/RWWA as set out in Table 5.2.2.3 and discussed earlier in this Report as :

- Base Stakes (specific owner percentage)
- Feature Stakes (specific owner percentage)
- Westspeed/Westbred/Westchase Bonuses
- Club Training Funds (designed to offset Racing Club and owner usage costs and maintain upkeep of facilities specific to training).

To therefore determine an estimation of the amount of funding provided by owners of horses and greyhounds for the WA Racing Industry on an annual basis, the total average annual operating cost per horse/dog derived in this analysis has been multiplied by the number of individual starters in the 2012/13 year. To this needs to be added the annual estimated investments made in new animals, again using 2012/13 estimated levels based on information from RWWA's Industry Status Reports.

On this basis the following estimated approximate annual net payments by owners in each Code are as follows (net of returns) :

	THOROUGHBRED	HARNESS	GREYHOUND	TOTAL
Annual Operating Costs	$76.5m	$34.3m	Nil *	$110.8m
Annual new animal purchases	$12.0m	$6.2m	$5.5m	$ 23.7m
TOTAL	$88.5m	$40.5m	$5.5m	$134.5m

*Returns to Greyhound owners on an operating cost basis only are estimated on average to be close to 100% of operating cost.

Accordingly, it can be seen that owners in net terms (net of returns) probably provide greater or roughly equivalent funding to the WA Racing Industry for producing and maintaining racing animals than the distributions injected by RWWA paid to Racing Clubs and participants from the operations of the WATAB in relation to annual product costs. Of course, it needs to be recognised that RWWA provides a range of other funding to the WA Racing Industry in addition to distributions as discussed throughout this Report, as well as the costs of racing operations and integrity.

This net funding by owners is what has been called by some as the "acceptable loss" of owners, ie. the accepted cost to owners of the pursuit of the largely intangible benefits of the dream of major success with a horse or greyhound, the social interactions, the excitement of attending the racing experience, the joy of a winning experience, and the sense of common purpose and involvement in the sport. By its very nature this level of investment therefore has a large discretionary component to it, and is significantly determined by the perceived opportunity or probability of achieving at least a reasonable level of return, as largely determined by stakes prizemoney.

Whilst as previously discussed the models of owners vary significantly, it is very clear that stakes prizemoney levels will significantly impact owners' involvement as follows:

- For larger and more financially orientated owners stakes prizemoney will more heavily and directly influence investment given the direct financial return implications
- For more hobbyist orientated owners the impacts of stakes prizemoney levels will be less direct and overt but will nevertheless determine overall preparedness to invest over time, particularly if there are reductions in stakes prizemoney.

It should be noted that the WA Racing Industry funding perspectives determined in this Report, whilst reflecting some differences, are generally reasonably consistent in context to the IER Report. The IER Report identified gross expenditure levels on wagering, preparing and racing animals, and customer expenditure. Taking the preparing and racing animals expenditure of $223.6 million in 2010/11 in the IER Report, this compares closely to the total figure of $224.5 million as the total expenditure figure by owners per this Report when the Annual Operating Costs (which is net of returns) of $110.8 million from the table above is added to the total racing distribution by RWWA of $113.7 million for 2012/13. Although a couple of years apart the general consistency of the figures indicate that these reflect reasonable indicative estimates of the funding of the WA Racing Industry.

5.2.5 **Infrastructure Funding**

The discussion to date on the funding of the Racing Industry in Western Australian has been in relation to operating expenditure. This section discusses the more problematic area of WA Racing Industry Infrastructure Funding. It is problematic because essentially the WA Racing Industry is generating only enough funding at present to break even on operations (with distributions and stakes prizemoney and other RWWA funding at levels just supporting this), with effectively little to no capability to meet infrastructure development or maintenance expenditure requirements.

Clearly the future development and sustainability of the industry is largely dependent on establishing, replacing and/or improving infrastructure at racing clubs to ensure facilities meet occupational safety and health (OSH) standards, licencing requirements, and the requirements of patrons.

At present, one source of funding for such expenditure is the Racecourse Infrastructure Grants Program (RIGP) established in July 2010 by the Western Australian Government, with an allocation of $13 million over 5 years (2010-2015). The aim of the RIGP is to support the establishment or improvement of infrastructure that is critical to the conduct of racing and/or training activities in both metropolitan and regional Western Australia. RIGP funding is offered on a partnership basis and as a general rule is only offered up to a maximum of 50% of the total project cost. The Western Australian Government provided further funding from the Royalties for Regions (R4R) program of $6.6 million in November 2012. As at 20 June 2014, RWWA advised that $9.7 million of RIGP and $2.9 million of R4R funding of the total $19.6 million of both combined had been spent, with RWWA adding further funding of $2.0 million to various projects.

Racing Clubs are then expected to secure the balance of funds required to undertake and complete projects from other sources, such as the Regional Development Commission, local government authorities, the Federal Government, RWWA, the Clubs' own resources, and/or from sponsorship. However, as explained earlier, Racing Clubs are facing significant financial pressures and finding it increasingly difficult to obtain other funding sources. Section 5.2.3 shows that Racing Clubs are barely breaking even operationally, any depreciation charged is largely inadequate or otherwise spent, and increased OSH and integrity requirements are expanding the required infrastructure expenditure beyond simply replacement and maintenance spend.

With the existing Government infrastructure funding programs set to conclude next year the question as to the continued funding of such infrastructure is unanswered at present. The concerns in this regard are compounded by a recent inventory of infrastructure spend requirements across the WA Racing Industry which is understood to have indicated a spend required of some $125 million. Whilst obviously an element of wish-list philosophy underpinned this listing, it nevertheless reflects the magnitude of this issue.

The 2008/9 review of the RWWA Act by the Joint Standing Committee on the Review of the Racing and Wagering Western Australia Acts under the chairmanship of Mr. John McGrath MLA, entitled "Inquiry into the Racing and Wagering Western Australia Acts, Report No 2, 2010" (the McGrath Report) suggested a reduction in the wagering tax with funds retained by RWWA from the WATAB channelled into an infrastructure fund to generate annual spend and ongoing contribution to a corpus for the future. Any privatisation of WATAB and resulting WA Racing Industry funding arrangements should encompass provision in relation to ongoing infrastructure funding requirements.

This could be achieved in a variety of ways such as:

- Factoring into any on-going distribution funding to the WA Racing Industry from WATAB, whether privatised or not, an additional and higher amount for infrastructure funding.
- If the WATAB is privatised a proportion of the sale proceeds could be allocated to an infrastructure fund.
- The existing cash reserves of RWWA could be allocated to an infrastructure fund.
- As suggested in the McGrath Report a reduction in the wagering tax with the amount of the reduction paid into an infrastructure fund.

An infrastructure fund, particularly if substantially seeded initially, could be used in a manner where investment returns, with a small annual release of capital, could then be supplemented by funding from the WA Government where public policy objectives were also part of the business case.

5.3 Code Value Chains

In properly understanding the implications of a potential privatisation of WATAB on the WA racing industry it is necessary to understand the value chains within each of the Racing Codes. It is only then that the Government can get a more accurate perspective of the effects of its decisions in this regard, and the WA Racing Industry will have a broader understanding of the potential impacts to its constituent parts. This Section of this Report attempts to outline key elements of the value chains of each of the Codes individually, recognising that in the time available for this study that this is a preliminary overview only of the important elements within these value chains, and the potential impacts of the potential privatisations of WATAB.

5.3.1 Thoroughbreds

As with the thoroughbred racing industries in all Australian jurisdictions (but arguably even to a greater extent in the relatively more isolated Western Australian racing industry), the cross-overs or joint involvements by participants in more than one part of the value chain is a feature in any discussion of the linkages and economic dependencies. The main groups directly involved in the thoroughbred racing industry are the breeders, the owners, the trainers, the jockeys, the stable staff, and the RWWA and Racing Club administrators. This latter group have been discussed elsewhere in this Report and won't be covered in this section.

The interconnectivity between the breeding, training and ownership activities are seen in the following statistics obtained in discussion with RWWA:

- 52% of the currently licenced trainers own a horse that started in the last 12 months (and this percentage would probably be substantially higher if horses owned by family members are included)
- 68% of thoroughbred breeders owned a horse that raced in the last 18 months.

Accordingly, there are limited examples of purity within elements of the value chain, and hence the following comments on the segments are made with this in mind.

5.3.1.1 Breeders

At its core the business model of breeders is to arrange a mare to foal, tend the weanling, and prepare the yearling for sale. Breeders will have their own stallions but will also look to service their mares with other stallions for the payment of a service fee. To facilitate this model many breeders will own their own property and some stallions and obviously a significant amount of broodmares.

Probably the best overall reflection of the difficult economic model faced by breeders in Western Australian is shown in the following table supplied by the Thoroughbred Breeders Western Australia (TBWA) outlining the average cost of bringing a yearling to sale in WA compared to the average sale price achieved at the main yearling sale in Perth.

	Average Yearling Cost	Average Sale Price	Cost vs Sale Price Averages
2007/08	$26,460	$50,514	$24,054
2008/09	$28,460	$38,247	$ 9,797
2009/10	$30,300	$41,659	$11,359
2010/11	$33,100	$44,639	$11,539
2011/12	$35,500	$38,170	$ 2,670
2012/13	$38,050	$39,367	$ 1,317
2013/14	$39,400	$39,916	$ 516

The average sale prices are taken from the main sessions of the Magic Millions primary sale in Perth, and largely reflect the figures as contained in RWWA's annual Industry Status Report. The average yearling cost is based on the costings calculated on a mare producing a foal and it being raised and taken through to a yearling sale in February/March of its yearling year. The basis of these costings are set out later in Table 5.3.1.1A (shown for the 2013 year with comparable figures for the 2008 year).

The table above clearly illustrates the contraction in returns to breeders in the Western Australian thoroughbred market flowing from a compound annual growth rate in cost over the last 6 years of 7% per annum, at a time of decline or certainly no growth in average sale prices being received.

This impact is then reflected in Breeding Distribution Statistics from the Australian Racing Fact Book 2012/13, which shows that the Western Australian breeding figures are falling quicker than the overall Australian figure. This is illustrated in WA's proportion of national stallions falling from 12.4% in 2009/10 to 11.1% in 2012/13, for broodmares the figures are 12.3% down to 11.7% for the same period, and significantly the proportion of the nation's foals fell from 11.7% to 9.6% from 2007/08 to 2012/13.

The stagnate yearlings sale environment is even further emphasised when the statistics for total yearling sales in Perth over the last 10 years (as provided by Magic Millions) are considered, as set out later in Table 5.3.1.1B. When total yearlings sold for the year are taken into account, the average prices achieved per year from the data in Table 5.3.1.1B are as listed below:

	Average Yearling Sales Price ($)
2005	23,834
2006	28,514
2007	30,844
2008	32,399
2009	24,600
2010	28,947
2011	30,254
2012	29,722
2013	30,069
2014	33,755

When these results are considered against the average cost of preparing a yearling for sale as listed in Table 5.3.1.1A for the corresponding years, the economic model on average for breeders is shown to be very tight. This is on top of the situation where there is a loss of around 30% of yearlings on catalogue for sales due to withdrawals from injury and passed in yearlings that don't sell at sales. This is also after about at least 5% of foals who do not make their first birthday.

Of concern more generally for the WA thoroughbred industry (and particularly breeders) is that when the aggregate on gross sales proceeds and average yearling prices for a number of Eastern State sales are considered (particularly the larger sales), there is generally more evidence of growth in these statistics. Some of the smaller yearling sales around Australia have exhibited equally challenging outcomes as the Perth sales, but with larger sales reflecting better results this is of concern to the WA Racing Industry. Under any potential privatisation of WATAB the incentives to breeders and buyers of thoroughbred yearlings, predominantly in the form of stakes prizemoney and incentive bonuses, need to be maintained and to continue to grow into the future.

TABLE 5.3.1.1A - BUDGET COST OF YEARLING (Conception to Sale)

All figures are net of GST

COMMENTS	NOTES/COMMENTS	BUDGET COSTS	2008 FIGURES
VET COSTS (AVERAGE PER MARE TO GET IN FOAL		$750.00	$500.00
VAN SERVE EXPENSES	STAFF AND FUEL COSTS OR TAXI	$500.00	$300.00
AGISTMENT FOR MARE (WHILST PREGNANT)	$24.00 PER DAY / 343 DAYS	$8,232.00	$5,488.00
FOALING DOWN FEE	SET FEE	$500.00	$300.00
**EXTRA AGISTMENT FOR MARE WHEN FOAL BORN	$2.00 PER DAY X 155	$310.00	$232.00
AGISTMENT FOR WEANLING (THROUGH TO YEARLING PREP)	$20.0 PER DAY X 270	$5400.00	$4,050.00
FARRIER WORK (MARE FOR 12 MONTH WHILST IN FOAL)	$40 PER TRIM	$240.00	$180.00
WEANING FEE (HALTER BREAK, HANDLING, STABLING ETC|)	SET FEE	$500.00	$300.00
FARRIER WORK (FROM FOAL TO YEARLING SALE)	$40 PER TRIM (17 TIMES)	$680.00	$510.00
FARRIER FOR SALE	1 SET OF SHOES FOR SALE	$135.00	$110.00
MICROCHIPPING	SET FEE	$100.00	$100.00
BRANDING	SET FEE	$100.00	$100.00
YEARLING PREPARATION	460 PER DAY (10 WEEKS)	$4,200.00	$2,520.00
RADIOGRAPHS FOR YEARLING SALE	SET FEE	$1,000.00	
PRESENTATION / ACCOMMODATION ETC FOR SALE	SHARED AMONGST DRAFT	$1,500.00	$1,000.00
YEARLING SALE ENTRY FEE	SET FEE	$1,300.00	$1,100.00
VET COSTS (\FOAL THROUGH TO YEARLING SALE)		$500.00	$400.00
INSURANCE FOR WEANING TO YEARLING	APPROXIMATE	$2,000.00	$1,500.00
MISC MARE EXPENSES		$200.00	$150.00
MISC YEARLING EXPENSES		$200.00	$150.00
WORM AND VACCINATION		$500.00	$350.00
MARE RETURN		$200.00	$120.00
SERVICE FEE		$9,000.00	$7,000.00
	TOTAL	$38,047.00	$26,460.00

GROSS INCOME		$50,000.00	$50,000.00
SELLING COMPANY COMMISSION	8.350%	$4,175.00	$4,175.00
NET INCOME		$7,778.00	$19,365.00

NOTES:

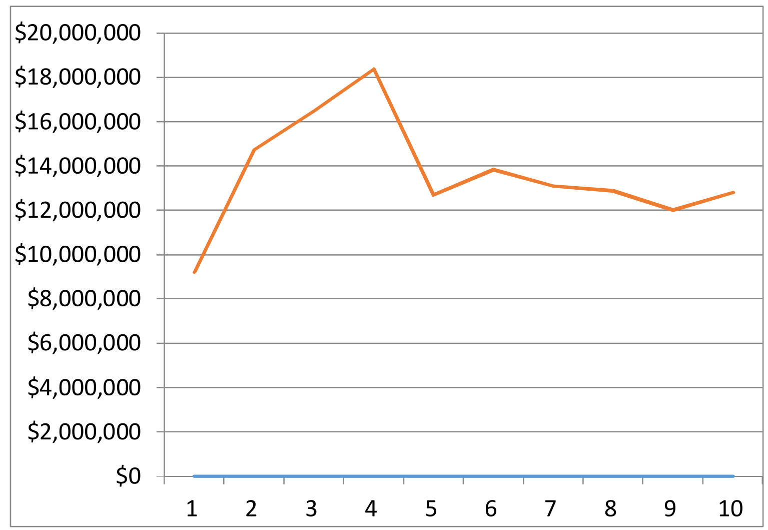
The costings calculated are on a mare producing a foal and it being raised and taken through to a yearling sale in Feb / March of its yearling year\
The costing are also worked out on average that a mare foals in around October, and a foal is weaned at 6 months approx. 1 April of the following year
*The van serve costings is based on the mare going in foal on the first attempt
**The extra agistment charge for the mare when the foal is born I only the 'gap' difference between a wet mare and a dry mare
**We assume that the mare is back in foal and that agistment coting is allocated to the next foal.
We have allocated agistment costs as a constant as although memb4ers with their own properties will have a base feed cost, they also have their labour, land holding expenses and property maintenance costs to consider.

TABLE 5.3.1.1B
MAGIC MILLIONS - SALE OF YEARLINGS IN PERTH 2005 - 2014

Year	Sale	Catalogued	Sold	Gross
2005	Perth Yearling Sale	505	374	$ 9,143,500.00
2005	Perth Winter Thoroughbred Sale	16	12	$ 56,500.00
2006	Perth Yearling Sale	634	472	$ 13,443,750.00
2006	Perth Winter Thoroughbred Sale	36	30	$ 1,230,450.00
2006	Perth May Monthly Sale	25	14	$ 38,900.00
2007	Perth Yearling Sale	675	510	$ 16,399,850.00
2007	Perth Winter Thoroughbred Sale	31	25	$ 102,100.00
2008	Perth Yearling Sale	787	519	$ 18,161,500.00
2008	Perth Winter Thoroughbred Sale	33	24	$ 134,900.00
2008	Perth Mixed Thoroughbred Sale	27	24	$ 73,900.00
2009	Perth Yearling Sale	440	305	$ 11,655,000.00
2009	Perth Westspeed Yearling Sale	361	184	$ 978,050.00
2009	Perth Autumn Thoroughbred Sale	8	5	$ 11,150.00
2009	Perth Winter Thoroughbred Sale	43	21	$ 55,100.00
2010	Perth Yearling Sale	630	434	$ 13,720,500.00
2010	Perth Autumn Thoroughbred Sale	52	38	$ 91,550.00
2010	Perth Winter Thoroughbred Sale	10	6	$ 24,450.00
2011	Perth Yearling Sale	686	407	$ 12,959,200.00
2011	Perth Autumn Thoroughbred Sale	12	6	$ 61,200.00
2011	Perth Winter Thoroughbred Sale	35	20	$ 79,700.00
2012	Perth Yearling Sale	580	405	$ 12,767,350.00
2012	Perth Autumn Thoroughbred Sale	18	16	$ 32,750.00
2012	Perth Winter Thoroughbred Sale	25	12	$ 69,500.00
2013	Perth Yearling Sale	415	290	$ 11,327,500.00
2013	Perth Autumn Thoroughbred Sale	35	21	$ 28,750.00
2013	Perth Winter Yearling Sale	133	85	$ 637,590.00
2013	Perth Winter Thoroughbred Sale	3	3	$ 3,700.00
2014	Perth Yearling Sale	415	311	$ 12,387,000.00
2014	Perth Autumn Thoroughbred Sale	23	17	$ 13,400.00
2014	Perth Winter Yearling Sale	65	49	$ 392,000.00
2014	Perth Winter Thoroughbred Sale	2	2	$ 650.00
TOTAL YEARLINGS SOLD IN PERTH BY MAGIC MILLIONS 2005-2014			**4641**	**$136,081,440.00**

TOTAL YEARLINGS SOLD BY YEAR

Year	Yearlings Sold	Gross
2005	386	$ 9,200,000.00
2006	516	$14,713,100.00
2007	535	$ 16,501,950.00
2008	567	$ 18,370,300.00
2009	515	$ 12,699,300.00
2010	478	$ 13,836,500.00
2011	433	$ 13,100,100.00
2012	433	$ 12,869,600.00
2013	399	$ 11,997,540.00
2014	379	$ 12,793,050.00



A thoroughbred breeder's broad financial model looks something like the following:

Income
Service Fees
Agistment
Sale of yearlings
"Acquisition of Ownership Stakes"

Expenses
Stock purchase (stallions and mares)
Service Fees
Mare/Weanling/Yearling Expenses (per Table 5.3.1.1A)
Property Expenses
Veterinary Expenses
Feed
Staff Wages
Other Expenses

In general terms for these income items, service fees in Western Australian are under pressure because of lack of depth and quality of the stallions, sales of yearlings have stagnated (but less yearlings generally), and acquisition of ownership stakes is really only transferring what should be breeding income into ownership of racehorses. As indicated earlier, breeders are very significant horse owners, often forced into this position to get a sale done because of the inability to sell otherwise. It should be said that this level of horse ownership by breeders is not a Western Australian phenomena, as reflected in the key findings of a report entitled "Breeders' Contribution to Racehorse Ownership" released by the Thoroughbred Breeders Australia in February 2010, which found the following on a national basis:

- 84% of breeders own racehorses
- Breeders have an ownership share in 63% of all racehorses in training
- When the ownership percentages of shares in racehorses owned by breeders is added together it equates to an equivalent of full ownership of 45% of all racehorses in training.

In Section 5.2.4 of this Report the returns to ownership were outlined, and hence such acquisition (or retention) of horse ownership is not on average a returning investment, reflecting limited overall returns from the WA Racing Industry for breeders when this is put alongside the challenging returns position from breeding.

In relation to expenses, Tables 5.3.1.1A in this section outlines the overall increases here. Later in this Chapter of this Report some of the specific expense areas will be discussed in more detail.

From discussions with thoroughbred breeders it is clear the Westpeed Incentive Scheme, including the recently introduced Westspeed Stallions initiative, is a major factor encouraging breeders to stay in breeding despite the difficult financial model outlined above. This is particularly so in the context of providing breeders with the opportunity to access an ongoing revenue stream from the yearlings they have previously sold, via their racing success. In a number of cases it was expressed that without such a scheme it was likely that the breeder would shut down. This program is providing the basis to at least enable breeders to compete at some level with the Hunter Valley and Victorian industry participants for stallions which would not otherwise be possible.

This Westspeed Incentive Scheme and the other RWWA distributions and funding that drive owners and others to continue in the WA Racing Industry must be maintained under a potential privatisation model.

5.3.1.2 Trainers

As with breeders the trainers' business model is in many cases intertwined with horse ownership. Trainers operate on what appears to be many different models, with the extent of horse ownership being the major differential to their financial models. This directly affects the proportionality of a trainer's income that is represented by Trainers Fee and their trainer's share of prize money as opposed to the extent of horse ownership stakes prizemoney. However, from discussions with trainers and from reviewing various profit and loss statements of trainers in differing positions in relation to the extent of horse ownership, it is clear that training fees levied to external owners at best only just meet the costs of training their thoroughbreds.

In general terms the financial model for trainers looks something like the following:

Income
Training Fees
Expenses reimbursed by owners
Trainers Percentage
Agistment
Stakes Prizemoney

Expenses
Pre-Training expenses
Feed
Veterinary expenses
Property expenses
Office overheads
Staff Wages
Other Expenses

Training fees for metropolitan/provincial trainers are currently around $70-$80 per day, with trainers at the lower end making essentially no profit. These training fees have increased from $60-65 per day in 2008, an increase of around 20-25% over those 6 years, or around 3.5% to 3.75% per annum. It is generally considered that there are too many trainers within the WA industry which therefore puts pressure on fee levels resulting in them being set at levels that provide little return to trainers. This is reflected in the ratio of thoroughbred training licences to horses that raced – a 6:1 ratio in WA in 2012/13 compared to 7-9:1 in the Eastern States. With owners expectations on fees conditioned by this position, trainers will often either use themselves or family members for strapping and other work on public holidays because it is otherwise too expensive if staff on penalty rates are used and owners will dispute bills, won't pay, and/or may move the horse to another trainer.

In the case of most country trainers, it is understood that they generally charge training fees of around $60-$65 per day, with extras at around the same as city rates. Given many costs would be around the same levels as for city/provincial trainers, the financial model would be very difficult.

The Trainers percentage of 10% of stakes prizemoney is obviously a variable source of income dependent on success and can't be relied upon but clearly helps to improve the books of trainers.

Depending upon the size of the operation and the extent of the horse ownership, these two sources (plus expense reimbursement by owners) can provide between around 75-100% of a trainer's income with large trainers able to enhance income at this lower end by agistment, and to a lesser extent stakes prizemoney from ownership.

The high levels of ownership of racehorses by trainers generally (although not in all cases) arises from a number of reasons, with the predominant ones appearing to include:

- Trainers buying horses at sales without committed owners and being left with unsold shares – which has been made more likely by the change in rule to allow 20 names of owners in the racebook (previously only 10) which enable owners to achieve their objectives of ownership with a lower investment
- Actively taking ownership percentages to entice owners to buy certain horses, or conversely requested by loyal owners
- Other objectives flowing from their broad involvement in the industry, such as supporting family member's involvement and/or employment in the industry.

Again, as with breeders, trainers face the similar horse ownership financial model as previously outlined, although clearly absorbing their share of the trainers fee through personal exertion. Whilst stakes prizemoney as owners helps to improve their income flow, the absorbed on average losses of horse ownership again just adds to the difficult financial model facing trainers.

On the cost side, some of these expenses will be discussed in more detail below, but with training fee increases only reflecting less than 4% per annum growth and RWWA distributions to participants exhibiting less growth than this, the training financial model is under pressure, with many struggling to meet their ongoing commitments, as in many cases cost increases are much greater than this.

Whilst trainer's financial models do vary significantly some general observations of the cost base and hence a context of operational outcomes are as follows:

- Wages would appear to constitute somewhere around 30-33% of a trainer's cost base when stable staff (roughly about one staff member to every five horses), track riders and the like are taken into account. As will be discussed later, the award rates for these staff has increased at around 23-25% over the last six years, and hence trainers fees increases have only just met these increases.
- Property costs range around 5-10% depending upon repairs and maintenance requirements.
- Veterinary expenses represent around 4-6% of total costs

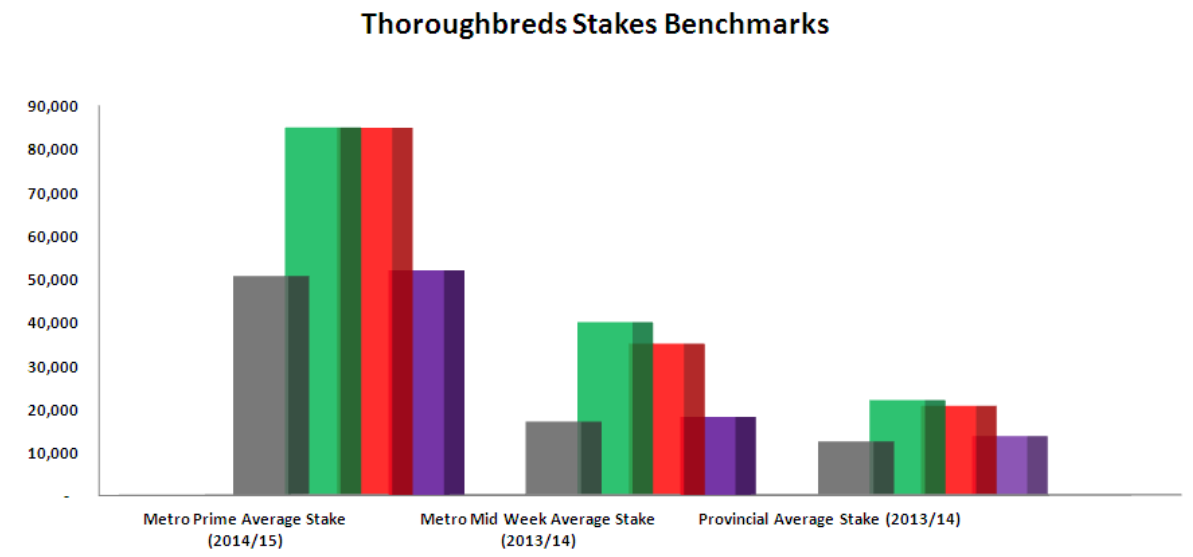
- Pre-training costs (such a breaking in, etc) can vary from 5% to more than 15% of cost depending upon the training business model in place and whether agistment / pre training facilities are owned or paid for externally
- Net profit or surplus before tax expressed as a percentage of revenue can obviously fluctuate fairly significantly but would appear to on average come in at between 1.5% to 4% of total revenue for those trainers that can generate a surplus, which does not represent a significant return in an operational sense, especially for the many who do not generate such surpluses given these are average numbers, and generally the figures do not include a wage for the trainer.

As the trainer's financial and business model relies on owners paying trainers fees and other costs of training and on the returns of horse ownership (whether a hobby or a business), the trainer is intimately tied into the economic model of horse ownership. This model was fully discussed in Section 5.2.4. As this ownership model is primarily dependent upon wagering funded distributions and other funding from RWWA for direct funding and for providing the incentive for owners to continue to invest for stakes prizemoney, the trainer's financial model is therefore similarly dependant and subject to any impacts that privatisation of the WATAB would have on that model. It can be seen that the training financial model works on small to no margins in an operational sense, with again property assets supporting operational provision and reflecting in most cases the only retirement wealth support/superannuation base for many trainers.

5.3.1.3 Owners

Owners are clearly a very widely spread group of participants in the WA Racing Industry with an equally varied set of financial and business models through which such ownership occurs. Section 5.2.4 discussed in full the owners' financial model in the WA racing industry and its positioning in the context of any potential privatisation. The diversity of owners ranges from those that fully own large numbers of horses (often including stallions, broodmares and yearlings) to those who hold a 10% syndicate share in one horse. In discussions with some of the larger owners it is quite common that a number of them have progressed to breeding as an extension of their racing industry involvement and to diversify across the value chain. In many cases it is also clear that other income sources outside of racing are what is funding generally a significant deficit on their racing involvement. Increased focus by the Australian Taxation Office on these involvements is an ongoing issue of potential risk to this source of funding to the WA Racing Industry.

In Section 5.2.4 the importance of the stakes prizemoney levels to owners' continued investment in the WA Racing Industry was also discussed. The Chart on the next page provides a comparison of average metropolitan and provincial thoroughbred stakes prizemoney across Queensland, New South Wales, Victoria and Western Australia. The chart reflects the large disparity from the major Eastern State markets, and some relativity to Queensland racing, although recently announced feature race prizemoney increases in Queensland will probably see this position change. Western Australia's average stakes prizemoney comparisons to major racing jurisdictions as reflected in this chart clearly evidence the need to maintain and provide ongoing improvement in levels of WA Racing Industry funding to remain competitive and ensure owners of WA thoroughbreds continue to invest in horses and fund the operations of the Industry.



	Metro Prime Average Stake (2014/15)	Metro Mid Week Average Stake (2013/14)	Provincial Average Stake (2013/14)
QLD	50,625	17,000	12,430
NSW	85,000	40,000	22,000
VIC	85,000	35,000	20,625
WA	52,000	18,045	13,625

5.3.1.4 Jockeys

RWWA's Industry Status Report of 2013 indicated that there were 88 jockeys and 38 apprentice jockeys registered in the 2012/13 year. These jockeys are paid by RWWA through the Racing Clubs. RWWA sets the jockey fee in negotiation with the WA Jockeys Association which for fully accredited jockeys is presently $172.50 per ride and for apprentice jockeys is also $172.50. Jockeys also get paid 5% of any stakes prizemoney paid to horses they ride, with this money for apprentices going into a Trust Fund for future access.

The Western Australian Jockey Association (WAJA) advises that of the around 90 jockeys registered with RWWA, about 1/3 of them are full-time jockeys with the rest being seasonal or part-time jockeys. Whilst some jockeys do a small amount of trackwork, nearly all of their income comes from race riding fees (with minor amounts from Engagement Fees on scratchings) and their 5% of stakes (although the stakes money income is dominated by a small number of major jockeys). On this basis the overall picture as described by the WAJA is that probably around 20 jockeys in the metropolitan area are generating reasonable returns from racing (reflecting earning in excess of $80,000 per annum), while the rest are in more difficult financial positions, particularly country jockeys who incur significant travel costs and equipment costs as their gear wears out quicker.

To expand on this further, from discussions with RWWA, it appears that in terms of looking at income bands applying to rankings of jockeys in groups of 10 from the highest group of 10 to the lowest group of 10, that only the top 30 jockeys (or the top 3 groups of 10 jockeys), earned an average income above what would be considered the minimum wage level in 2012/13.

Many outside of these are either seasonal or part time riders. There are 30 jockeys who are predominantly country riders, some who move about to ride all year round and some who just ride in the region's racing season. Only around 6 of these country jockeys earned above what would be considered to be the minimum wage level in 2012/13.

Apprentice jockeys have the same financial model as jockeys (except for some initial travel assistance from RWWA). It would appear that around half of them would have earnt around the minimum wage level in 2012/13. It is understood that around 20 of the 38 rode for the entire season.

The financial model for jockeys is their income as outlined above, and expenses which encompasses travel costs (drive, fly, accommodation if necessary) which are very rarely reimbursed by Racing Clubs, race and track riding gear costs, and discretionary sports medicine type expenses such as physiotherapy, personal training, weight loss systems, as well as personal accident / income protection insurance, etc., RWWA have increased funding in terms of meeting the costs of a sports doctor and psychologist being available to jockeys, paying medical expenses and workers compensation insurance, race meeting accident and public liability insurance premiums, and paying superannuation (in lieu of an increase in the riders fee). It should also be noted that jockeys, whilst covered by RWWA's Workers Compensation Insurance, are not employees and consequently do not receive annual or personal leave.

In a general high level financial assessment of jockey's income position in Western Australian based on 2013 figures, the following calculation was undertaken

				Per Jockey/ Apprentice (126)
Starters in Races (23,364) X $172		=	$4,018,608	$31,894
5% Jockeys Percentage	X Total Stakes ($50,361,907)	=	$2,518,095	$19,985
			$6,536,703	$51,879
			=========	=======

Based on this calculation (which is obviously only a very high level estimate), and clearly has no allowance for any workers compensation payments received, on average jockeys are being paid around $32,000 annually in riders fees. It is interesting to compare this to the minimum wage rate for a trackrider under the Horse and Greyhound Training Award which currently would establish a minimum annual payment for an adult trackrider of around $35,600. Whilst clearly there is the capacity for jockeys to enhance this through the percentage on stakes prizemoney, this would generally fall to a smaller number of jockeys, and hence for a large number of jockeys pay rates are around what could be considered to be minimum wage rate levels.

5.3.1.5 Staff

Breeders, trainers and some owners employ a number of people to work in their stables and other operations. The IER Report indicated there were 2,614 Breeders Staff and 422 trackriders/stablehands employed in the Western Australian thoroughbred industry. There are also many casual workers employed across the industry from time-to-time, including backpackers and the like.

In the context of understanding the financial perspective here, Appendix 2 to this Report is the current Horse and Greyhound Training Award minimum wage rates across various classifications, which range from adult rates through to rates applying to employees down to 15 years of age. To illustrate the cost pressures flowing from this group, adult rates for Stablehand – Grade 1 and Stable Foreman were obtained for 2008 and 2014 for single time and Sunday Casual rates as follows:

	Single Time		Sunday Casual	
	2008	2014	2008	2014
Stablehand – Grade 1	14.08	17.35	35.20	43.38
Stable Foreman	15.94	19.64	39.86	49.10

The increases in these rates across that time have been 23.2% for both Single Time Stablehand and for Sunday Casual, and for the Foreman the increases were 25% and 23.2% respectively. This increase equates to around 2.75% per annum compounded over the six years and given the significance of this cost to these operations has worked to put pressure of the financial models of participants in the WA thoroughbred racing industry.

Breeding staff would appear to be covered under Agricultural or Pastoral Farm Awards to which the Minimum Conditions of Employment Act 1993 would seem to apply. As the pay rates in accordance with this Act currently applying are similar for single time adult employment as the rates above, it is assumed that this situation also applies to breeders.

5.3.2 Harness

As discussed in relation to the thoroughbred racing industry in Western Australia, the value chain of Western Australian Harness racing is also extremely interwoven with high levels of ownership of horses held by breeders and trainers. Data provided by

RWWA indicates that around 68.5% of Breeders Groups of standardbreds raced a horse in West Australia in the past 18 months, or if focused to individuals rather than groups their percentage was around 56%. In relation to trainers the following statistics reflect the extent of ownership.

- Approximately 76% of harness racing trainers raced a horse they owned in the last 18 months.
- Approximately 44% of horses that raced in the last 18 months were owned in some sort of ownership configuration by their trainer.

So again the value chain discussion reflects a large degree of this cross-over throughout the harness racing value chain.

5.3.2.1 Breeders

According to the IER Report there were around 1,860 harness racing breeders in WA (assuming an average of 2 breeders per broodmare) in the 2010/11 year. It is estimated that over 90% of these were hobbyists, with only a handful of full-time breeders. Breeding of a harness racing horse is essentially a four year proposition which needs both confidence to invest and the ability to meet the financial commitment over that period.

From discussions with the Breeders Owners Trainers Reinsperson Association (BOTRA) it was advised that only about 50% of foals end up racing.

The low returns and tight economics for harness horse breeding is reflected in a number of fairly damning economic and business statistics for harness racing breeders :

- From RWWA'S Industry Status Report 2013 the amount of Standardbreds born in WA in 2012/13 was 459, down from 659 the previous year
- This drop-off in breeding is reinforced by advice from RWWA that in the last 18 months just 263 Breeding Groups, consisting of 434 individuals, bred a Standardbred foal in Western Australia
- Whilst the average yearling price achieved in 2012/13 was $13,517, which grew from $10,829 the year before based on figures in RWWA Industry Status Report 2012/13, this is still below the $15,000-$20,000 estimated cost of getting the horse to the sales.
- This average yearling price in 2012/13 clearly reflects the scarcity value of the drop off in local breeding, given average prices of just $9,071, $10,120 and $10,829 in the preceding three years (per the same Industry Status Report).

The cost base for harness breeders reflects costs similar to those of thoroughbred breeders, with the major costs being :

- Property costs – some breeders (mainly the larger ones) own property for breeding purposes and some agist.
- Veterinary expenses
- Farriers
- Transport
- Feed merchants
- Harness equipment

As with thoroughbred breeding, these costs (as will be further discussed later), have in nearly if not all cases escalated at rates in excess of the increases in distributions (stakes), and particularly greater than the returns through sales proceeds to local breeders. This can be seen in the declining total sales proceeds over the last five years as follows (from RWWA's Industry Status Report 2013) :

	Standardbred Sales Proceeds ($M)
2008/09	8.717
2009/10	5.878
2010/11	6.497
2011/12	7.136
2012/13	6.204

RWWA's Westbred incentive bonus scheme has played a critical role in steadying the declining investment proposition faced by harness racing breeders (and owners as well) by providing early cashflows for Westbred foals, and also credits under the EPONA Mares Bonus Scheme.

Nevertheless, the difficult financial model here, and the hobbyists/cottage industry nature of local breeding in harness racing in Western Australia has seen a significant number of Eastern States and New Zealand horses being brought into the State to uphold the quality and size of the harness racing product.

The ability and propensity to bring these horses in lies largely in the stakes offered in WA harness racing being at very competitive levels relative to interstate stakes levels eg; when compared to Victoria they are about 120%-124% of comparable Victorian stakes levels, other than for midweek metropolitan races which are at essentially the same levels ie, 100% of Victorian stakes levels. This position is obviously supported by the stakes distributions made by RWWA, and it is interesting to note that harness racing's share of distributions to the WA Racing Industry is 26.2% of the total, whilst its contribution to wagering turnover on just WA racing is only 19%, and around 16% of total betting on racing through WATAB. With no ability for Harness Racing Clubs to top up the RWWA stakes distributions because of their parlous financial position, harness racing in Western Australia is totally dependent upon the continuation of distribution and other RWWA funding levels at current levels, with breeders obviously facing difficult breeding financials and with their significant horse ownership levels on average further deteriorating this position.

5.3.2.2 Trainers

As outlined earlier, harness racing trainers are very substantial owners of horses through syndication. Trainer's business and financial models vary widely with some also being breeders, and often they are drivers as well. It is therefore not possible to make a generic assessment of the trainers' part of the value chain given that trainers will generate income with widely varying compositions from :

— Breeding – sale of horses
— Agistment
— Training fees
— Driver fees
— Stakes prizemoney

It is understood that there are around 7 leading trainers that generate strong and well above average returns which effectively more than proportionately reduces the amounts available to be spread over the rest in the industry, which is a substantial matter for these others given the 238 trainers and 370 driver/trainers registered with RWWA.

WA harness racing training fees are around $50-$55 per day, which when considered against the similar cost base structures and pressures discussed for breeders and for thoroughbred trainers, suggests that the trainer's percentage of stakes prizemoney at 7.5% of any such stakes is an extremely high dependency for trainer's financial positioning given the low level of training fees.

Accordingly, training in its own context is not a high return generator, if at all. This is reflected by the situation where the leading trainer in the State with over 200 winners (the first time this has ever been achieved) was only able to generate a very minor profit when considered against the stakes prizemoney these achievements represented.

The extent of trainer's horse ownership holdings varies significantly meaning the extent to which this draws on their financial position and further leverages their dependency on overall stakes and distributions levels equally varies. However, again, the overall horse ownership contribution as discussed in Section 5.2.4, with the high horse ownership position of trainers, places significant pressure on trainers' general financial model.

The position of drivers will be discussed below, but with driver/trainers representing around 80% of the industry's drivers this is the dominant model for harness racing driving in the WA harness racing industry. This clearly absorbs the income (and costs) profiles of the driver into the overall training financial model, with a driver's income being the driver race fees and the 5% of stakes prizemoney.

Therefore, with such a high ownership penetration, and low training fees, it appears that the majority of trainers do little more than break even on operations after extracting a living, based again on the relatively high stake levels provided in WA harness racing, with limited room to absorb any less funding without relatively immediate reductions in size, with this obviously being most immediate for those not in the top 7 or so of trainers.

5.3.2.3 Drivers

The drivers' income model is comprised of the RWWA funded race fee of $60 plus 5% of stakes prizemoney for a first three finish. Taking a similar analysis as performed for jockeys, the total number of registered drivers in 2012/13 was around 440, there were 23,169 starters, and total stakes prizemoney was $22.235 million. So estimated returns to drivers in total was :

		Returns to Drivers
23,169 X $60	=	$1,270,140
5% X $22.235 m	=	$1,117,750
		$2,387,890

If this is divided by 440 (the number of registered drivers) the average income per driver is around just $5,430, reflecting an average of just 48 race drives per driver. This is clearly highly misleading given that discussions with a leading driver only (ie, not also a trainer) indicated that he goes to every meeting he can and would drive in 900-1000 races annually. Again, a handful of drivers (and driver/trainers) will generate reasonable returns (and take a good part of the amount available for drivers' percentage), whilst a large number clearly undertake the involvement as a hobby. Continued funding by RWWA, particularly paying drivers, is critical in supporting the current industry in what is clearly a low wage/low return situation for drivers who need to meet all their own travel and motor vehicle expenses, racing attire and safety gear costs, and personal medical and accident insurance costs, together with the administration costs in organising their drives.

5.3.2.4 Owners

Section 5.2.4 outlined the financial model facing harness racing/standardbred owners on average – a model reflecting the concept of acceptable loss. Stakes levels being on average between around 16-24% above Victorian levels and at or above levels around Australia generally reflect the need for the stakes levels in Western Australia to meet the costs of this Code, and hence keep owners in harness racing in the State. Ownership numbers in WA harness racing on any measure have shown significant decline over the last five years. Depending upon the exact ownership definition the decline will vary, but in general terms it seems to be around 13-15% over the period.

Given the return ratio discussed in Section 5.2.4, the current WATAB/RWWA funding levels (including Westbred incentives) are necessary to keep this decline in ownership from accelerating.

5.3.2.5 Staff

The IER Report identified in 2010/11 that there were around 972 and 286 people employed by breeders and as trackriders/stablehands respectively in harness racing in Western Australia. As the same matters raised with thoroughbred industry staff apply to harness racing staff this will not be further discussed here.

5.3.3 Greyhounds

The value chain for greyhound racing is even more co-mingled than for the other Codes, with high levels of integration across breeding, training and ownership of greyhounds. In broad terms it would also appear that there are 3 to 4 trainers taking a large proportion of the stakes prizemoney available, particularly in metropolitan racing. The Greyhound racing industry in WA has in more recent times been challenged by the uncertainty associated with the position at Cannington and its funding. Whilst not fully resolved the provision of $13 million from RWWA has provided an ability to move forward, albeit with some temporary arrangements until fully required funding can be achieved.

5.3.3.1 Breeding

The IER Report identified 99 greyhound breeders in Western Australia in 2010/11, but it is unclear how many of these were also trainers and/or owners. There has been declining numbers of greyhounds born in WA over the last 5 years, declining by over 25% over that period. The decline and the lack of returns for local breeders is reflected in the position that in 2012/13 WA bred greyhounds made up only around 33.5% of all the unique runners in WA races (just 613 of the 1,828 unique runners), although part of the reason for this would probably relate to the uncertainty over Cannington as referred to earlier impacting local breeding, which could partly turn around given some degree of a way forward now.

The economics of greyhound breeding in Western Australia appears to be generally underpinned by the Westchase Incentive Scheme. Bonuses under this Scheme are paid to the owners and breeders of all WA bred greyhounds based on winning certain race classes and/or types, and is non-contributory for industry participants. This scheme, together with stakes prizemoney at the levels they are currently (70-75% of Victorian levels for city, and 120% for country and provincial) is underpinning not only the locally bred but also the importation of a large number of Eastern State bred greyhounds.

5.3.3.2 Trainers

RWWA's Industry Status Report 2013 identified 249 registered greyhound trainers, whilst the IER Report identified some 295 trainers in 2010/11 which was around the level in the RWWA Status Report for that year. The common financial model in greyhounds throughout Australia, and particularly so in Western Australia, is for trainers to take a 50% share of a greyhound with the owners, charge no training fees, and equally share the ownership rights and obligations (with variations between trainers on items such as veterinary costs or trial expenses). This very strong attachment to greyhound ownership and the "partnership" model with owners places trainers close to the greyhound ownership economics in an operational perspective, and in many cases essentially a total ownership sense if the "capital" cost is incorporated into the partnership.

In discussions with industry representatives it was established in their view that there were around 20 professional, full-time trainers. This indicates a significant number of part-time and hobby trainers and trainer/owners who will largely be involved in these roles for purposes of personal enjoyment and occasional track success largely within a cottage industry environment, based on current distribution and other RWWA funding levels. However, this industry picture needs to be seen in the context of a dramatic fall of over 15% in 2012/13 of the number of greyhound trainers, coupled with the substantial drop in greyhounds born.

The cost base of greyhound trainers again reflects a number of similar items to the horse trainers' position, with fuel and transport, feed, veterinary, power/water, and registration fees the major cost items (see Section 5.3.4). With no significant changes in stakes prizemoney over the last five years until 2012/13 (that year to bolster provincial racing), these costs had been increasing with no commensurate change in the inflows to the participants, putting pressure on both the trainers and owners financial position under the 50/50 structure.

To the extent that breeder/trainers and/or trainers have their own properties on which to raise and/or train greyhounds, these properties generally represent their retirement (superannuation) plan. Given however that these properties will be sold with the kennels and track the value of this property nevertheless lies more so in having a sustainable greyhound racing industry in Western Australia.

5.3.3.3 Owners

With trainers and owners subject to this cost escalation (see Section 5.3.4 below) without movement in stakes to those levels, the current balance within the greyhound industry financial model (which contains a large proportion of cottage industry participation), offers minimal flexibility for changes in stakes levels, bonusing and overall wagering operator funding under a potential privatisation model.

In Section 5.2.4 the Report discussed the position of owners, which reflected a clearly better net investment position for greyhound owners than in the other Codes. Despite the greyhound code distributions representing 13.1% of total distributions, whilst generating approximately 21.7% of WA wagering turnover on WA racing and around 31% of total racing wagering turnover of WATAB, the stakes prizemoney paid continues to attract local and imported dogs (either pups or ready to run) of around 915 per annum, with an ever increasing proportion of imported greyhounds. This wagering performance reflects the current situation in which in Western Australia there are six meetings per week broadcast by Sky Channel predominantly focused to drive wagering revenue.

5.3.4 Other Major Costs Items / Other Industry Stakeholders

There are a significant range of suppliers to the WA racing industry that impact these value chains and who are also therefore stakeholders in the industry and its funding model. There are a number of these stakeholders that have less direct dependency in their business model specifically on the WA Racing Industry, such as the power / gas / water utilities, transporting and freight, motor vehicle and fuel providers, and the events industry generally. For these suppliers the cost / charges escalation rates faced by the WA Racing Industry are understood from these suppliers' general price increases experienced by businesses generally – electricity around 10% this year and expected future higher increases, water price increases of 47% over 3 years to 2011 and 6% last year, motor vehicle service costs up 56% and petrol prices up 42% in the last 5 years, are examples of this. More specifically to the WA Racing Industry are costs such a veterinary expenses and feed expenses, discussed below :

(a) **Veterinary** – typical metropolitan based veterinary average invoice bills over 5 years to 2013 have increased by around 35% or over 6% per annum for thoroughbred and harness racing horse treatments. These average invoice levels fall significantly in the winter months as a result of the inability / unpreparedness of trainers particularly to incur such costs and then try to charge owners when stakes prizemoney are at their lowest and less racing is occurring. Accordingly, in winter lesser quality horses may not get treatments they perhaps should/would have received at other times, lower numbers of horses are put into work to reduce the spend, and without the types of stakes prizemoney available as in summer the winter spend drops.

Veterinary businesses can make losses at this time, and at times will decrease prices if necessary to help out during this period.

This reflects the sensitivity of the WA Racing Industry to the stakes prizemoney levels funded from wagering and to the tightness of the financial model. As some of these observations flow from a very large veterinary operation with 12 full-time staff and a number of casuals, such financial sensitivities and the reliance on veterinary suppliers by the WA racing industry is very clear to see, making such expenditure unavoidable despite the significant increases in cost.

(b) **Feed Industry** – the table below, provided by one of WA's largest equine feed supply businesses, shows the extent of the product/service price increases and their running cost escalations over the last 5 years.

Feed Industry Costs

Product / Service	2014	2009	% Increase
Chaff	34	32	6%
Chaff Rough Cut	23	19	21%
Lucern chaff	26	21	24%
Lucern Hay	22	16	38%
Hay	15	10	50%
Oats	17	15	13%
Horse pellets	18	16	13%
Oats Flaked	16	14	14%
Pony Cubes	26.5	24.5	8%
Stamazine	174	158	10%
Blue Muesli	31	23.85	30%
Megavite B 230ml	98	83	18%
P|egasus Studmaster	23.5	21	12%
Girth Exercise	54	39	38%
Sursingle Exercise	43	32	34%
Breastplate Exercise	40	36	11%
Running Costs			
Office Staff P/Hr	26	20	30%
Delivery Drivers P/Hr	23	18	28%
Counter Staff P/Hr	26	21	24%
Vehicle Service	700	450	56%
Fuel Litre	1.6	1.13	42%

As a significant cost component for all WA Racing Industry participants, these indications of the extent of cost pressure for the participants, which in a general context clearly exceed the increases in stakes and distributions paid to the Industry over this period funded by WATAB/RWWA, provides a further illustration of the squeeze to the Industry's financial model and value chains in recent years.

(c) **Magic Millions** – another important barometer of the WA Racing Industry, in this case for the thoroughbred industry, is the yearling sales performance conducted by Magic Millions. Magic Millions make a significant investment in the cost of running the sale and extend finance to all buyers on varying terms and lengths depending upon the buyers' history. Magic Millions revenue is generated from their selling commission of 8.35% of selling price.

The overall sale gross value achieved over the last five years had fallen from $13.721 million in 2010 to $11.328 million in 2013 with a slight rebound in 2014 to $12.419 million (due to a higher clearance rate but relatively flat average yearling sale price). There are less buyers apparent, with trainers generally identified as buying less than previously (some up to 50% less), again reflecting the earlier comments on their financial model difficulties.

The fragility of this element of the WA Racing Industry is evident from discussions with Magic Millions that suggest the sale event is potentially at risk with uncertainties around Belmont and the potential implications to the funding model of the WA Racing Industry of a privatisation of the WATAB. Some clarity and stability could call forward investment by Magic Millions in a new selling complex in Perth.

(d) **Industry Staff** – throughout this section the staffing stakeholders have been discussed, with breeders having staff in all 3 codes with trackriders and stablehands in the case of thoroughbred and harness racing codes.

Using the relevant Awards as representative of this Group it has been identified that the wages of this Group in general terms will have increased by some 23-25% over the last six years, with allowances, shorter working week and superannuation adding to these figures to some extent. As in some cases staffing costs can represent up to 30% of the cost base of breeders and trainers (but also some owners incur such costs), this also reflects the underlying cost pressures on significant parts of the value chains of these Codes, but more so for the thoroughbred and harness racing codes.

It is also very important to again point out in this regard that the Western Australian Racing Industry is one that provides a capacity to employ people that in many cases would have difficulty in finding employment elsewhere. With the protection of an Award, and with the ability to employ full-time people at 15 years of age, the importance of this to the Western Australian economy and to the employment of people throughout the State, should not be understated.

In a State where the mining industry, as a major employer, has seen the number of people employed fall by some 13% in the last year, a decline in WA Racing Industry employment together with reduced opportunities elsewhere (if such people could possibly look elsewhere) caused potentially by a reduced funding model under a possible privatised TAB would hurt the State significantly, in both metropolitan and regional areas.

Not only does the discussion in this section on suppliers to, and staff within, the WA Racing Industry further illustrate the challenging financial model for the industry participants, but it also clearly reflects the dependency of these suppliers on a sustainable WA Racing Industry. These suppliers, along with the WA Racing Industry participants, have continually absorbed the financial squeeze of costs growth exceeding racing industry income flow growth, and hence these suppliers have expressed the same concerns as to the certainty of the industry funding model under a potentially privatised WATAB.

5.3.5 Distribution Growth Rates Vs Cost Base Increases

At its simplest level, if the increases in RWWA distributions between 2008/9 and 2012/13 are compared to some of the cost increases in important inputs to the WA Racing Industry over that same period the following picture emerges:

	% Increases 2008/9 – 2012/13	CAGR 2008/9 – 2012/13
Total Racing Industry Distributions	5.27%	1.3%
Thoroughbred Distributions	7.23%	1.8%
Harness Distributions	-1.13%	-
Greyhound Distributions	1.52%	2.5%
Staff (Horse and Greyhound Training Award 2010)	23.2%	3.5%
Veterinary	35.0%	6.0%
Feed and Produce	say 20.0% on average	5% approx.
Utilities	26 – 46%	6-10%
Motor Vehicle	Say 50%	10.8%

This summation of the various elements talked about in the value chains of the WA Racing Industry Codes earlier in this Chapter of this Report reflect that the WA Racing Industry generally has continued to adapt and absorb cost increases well above the wagering based distributions increases that have been provided by WATAB/RWWA. This has been explained in some detail above, reflecting that industry participants have, in the main, operated on reducing contributions from racing activities, with a preparedness of all participants, but particularly owners, to continue in the WA Racing Industry for a variety of reasons including personal interest, for employment, for family sustainability in the industry, for continuity of the sport, and in some parts of the value chains, to hopefully build a retirement nest egg in many cases.

This Chapter does also clearly illustrate, however, that this continued investment and involvement is being continually and significantly challenged by the squeeze of cost pressures well in excess of growth in returns and funding to the WA Racing Industry. Such cost pressures and the need to adjust to these is not peculiar to this industry, but this Chapter reflects that the WA Racing Industry is not one that generates significant wealth to its participants, with a great deal of these tight financial models within the

WA Racing Industry actually funded from sources external to the racing model. Any potential privatisation of WATAB must ensure a "no worse off" position for the overall funding of the WA Racing Industry given this situation.

5.3.6 Investments in Property

Clearly the racing industry requires a significant amount of property on which to conduct its production and training of its product, outside the race tracks required to put on the racing product events. Accordingly, many breeders and trainers, and some owners, have acquired properties on which to conduct their racing activities.

In most cases, particularly with trainers, such properties effectively represent their superannuation investment given the racing operating model leaves little room for any substantial other form of retirement saving. The value of such properties with the accompanying investment in the appropriate infrastructure will be maximised and maintained only with ongoing performance of the various WA racing industry Codes. It is therefore important to understand that what may appear to be an asset-rich position is firstly not supported by a commensurate operational cashflow position, and secondly that best value is underpinned by ongoing industry sustainability. Whilst property will hold value in alternative use, particularly those in metropolitan areas, best value in many cases would appear to reside in continued use.

This issue is particularly relevant in any considerations of asset utilisation across Racing Clubs, and in the potential privatisation of the WATAB, with the latter perspective being one of requiring that the industry funding model is such as to ensure the WA Racing Industry is "no-worse off" to maintain its sustainability.

What Could Privatisation Of WATAB Look Like?

This Report to date has provided an outline of WATAB and RWWA, the wagering market in which it operates, discussed what privatisation involves and how other TAB's in Australia have been privatised, and outlined the current WA racing industry structure and funding under the current arrangements.

This chapter of this Report will discuss the various issues and options that could arise from the privatisation of WATAB. Just as there has been no single model for previous TAB privatisations in Australia, there is a myriad of different forms that the privatisation of WATAB could take in terms of structures and detailed financial flows.

6.1 Background

The major focus of this privatisation discussion will be to the WATAB, the wagering division of RWWA, in the context of the privatisation. However it is not entirely clear whether this consideration in some shape or form is to apply to the totality of RWWA. That is not to suggest that the PRA/Racing responsibilities of RWWA would be sold with the WATAB if a privatisation was to occur. It is purely to raise the prospect that a model similar to the Racing Victoria Limited (RVL) structure could be considered – RVL is an unlisted public company with no government ownership or enabling statute, save for its positioning within the joint venture requirements that sit within the Victorian wagering licence issued by the Victorian Government currently to Tabcorp.

RWWA is, as outlined earlier, a corporation established under statute but is not an agent of the Crown and can be sued, contracted with and otherwise dealt with as an entity without government protection, although it has a number of obligations to the Minister under the RWWA Act. Racing Victoria Limited is an independent unlisted public company limited by guarantee with 4 equal shareholders – the Victorian Racing Club, the Melbourne Racing Club, the Moonee Valley Racing Club, and the Victorian Country Racing Council, with many other thoroughbred industry stakeholders, ie, it does not represent all racing codes, just thoroughbred racing.

If the wagering functions were to be separated out of RWWA and sold as the WATAB, the WA Government will therefore need to determine what structure to put in place post the WATAB privatisation for the remaining functions of RWWA.

Without dwelling too much on this issue, it is instructive to quickly review the formation of RWWA in this respect. The major impetus for forming what became RWWA under the RWWA Act was the Turner Report determination that the governance arrangements of racing and wagering activities in Western Australia were not effective, and the recommendation of the Turner Report was that the principal club and controlling authority responsibilities of the three Codes and the TAB be formed into one co-ordinated body – later to become RWWA. The Turner Report at page 6 said "The role of the TAB was probably dysfunctional in terms of the interest of the industry at the time". This integration was unique in Australia, other than for a short time in Tasmania.

In general the McGrath Report found support for this structure and formed a view that the consolidation had been a good outcome. It needs to be understood that the interests of wagering and the interests of the racing industry are not necessarily always aligned and in fact in a number of instances can be in conflict. This is particularly so for example in the context that a racing program that ensures support and exposure for regional racing to underpin the racing industry's objectives is unlikely to necessarily match a program that optimises wagering revenues.

These potential conflicts have been essentially embedded within the decision making processes of the RWWA Board and Management as both sides of this debate are inhouse to RWWA. Privatisation of the WATAB would externalise this and requires structural and operational practices to be put in place in the legislation and licence to underpin the privatisation of the WATAB.

It has previously been acknowledged that RWWA has generally performed reasonably well in recent times, particularly in relation to wagering. In drilling down with stakeholders on this general satisfaction with RWWA's performance, much relates to the distribution and funding levels that have been provided, particularly those to racing industry participants. Racing Clubs had not generally been as positive on this front in terms of their distributions, although the $5 million in additional OSH related distributions paid late in July this year were warmly received. It is however interesting to note that such distribution and general funding levels have clearly been supported by good wagering growth rates by WATAB/RWWA as noted earlier.

The observation in this regard, reinforced by a number of participants' commentary, is that RWWA has probably prioritised its attention in recent times to the wagering part of the business to a significantly greater extent than its PRA obligations. This is not to say these racing responsibilities have been totally neglected but RWWA would have appeared to strategically focus on pushing the wagering business to generate such funding, reinforced by the "scare" of the reduced distributions in 2009/10. It is suggested that this has manifest itself in many ways, including:

- Significant investment directed to wagering systems (both retail and digital) and the retail wagering offer
- An under investment in a number of parts of the racing operations responsibilities, which it is now believed are being addressed flowing from RWWA's recently determined 7 areas of strategic focus in this regard. From discussions with RWWA management it is understood that this will result in increased operating and capital expenditure in a number of specific racing areas into the future, rectifying some of this previous underspending in these areas (which nevertheless has provided more funds for distributions and other funding in recent times).
- Statements and actions that suggested a view held by RWWA that their role was primarily to provide off-course betting and retail outlets, and that neither on-course betting nor necessarily promotion of the sport were its focuses, and that its role was not to provide funding for any upgrade of facilities for customers. One manifestation of this has been the substantial decline of on-course wagering at racetracks throughout the state, which overall has declined by nearly 25% in the last 5 years to 2012/13, and by a stated approximate 50% at Perth Racing's two metropolitan tracks in that time period. Whilst as discussed earlier there are a number of reasons for this decline in on-course wagering, including declining attendances, corporate bookmaker competition, and the general regulatory environment for wagering and on-course entertainment provision, RWWA's focus on off-course wagering can be seen to have contributed to this as reflected in the following examples:

- RWWA promoted and heavily advertised fixed odds betting side by side with tote odds in retail outlets but this was not made available to Racing Clubs.
- An apparent lack of preparedness by RWWA to facilitate call betting or more user friendly on-course bet slips for on-course betting
- Wagering information displays on-course have significantly lagged that offered to punters in retail outlets nor been adapted to the specific on-course environment.
- On course mobile offers have been inefficient and the introduction of tracking solutions to ensure appropriate revenue flow to Racing Clubs has been a drawn out affair.

All of these reflect the difficult position that RWWA has been placed in through having the dual roles associated with PRA responsibilities and its TAB wagering responsibilities. As stated above, these will often conflict in direction as each will have differing optimisation stances on many issues affecting the racing program and its conduct. So whilst RWWA has generally performed adequately in dealing with this difficulty, the sustainability of this situation can be questioned, particularly as the WATAB continues to need to actively confront the competition in the wagering industry in Australia. This is an issue whether or not privatisation of the WATAB proceeds.

It has been an observation of a number of industry participants that RWWA's approach to these conflicting objectives appears to have more recently shifted to a more balanced perspective on many matters as it embraces the needs to promote the racing sport and the Racing Clubs, and on-course wagering. RWWA has acknowledged this as flowing from its recent strategic planning exercises. Some participants in the WA Racing Industry note the timing being at around the same time that more active discussion began on the issue of the potential privatisation of the WATAB. This again reflects the difficulty for Board and Management of these two functions being under one roof.

If the WATAB (RWWA's wagering operations) is privatised then the PRA and other racing responsibilities could stay with RWWA, perhaps renamed Racing Western Australia (RWA), under its current (but obviously amended) legislation or other structures as outlined throughout this Report. All other States and Territories have corporatised statutory bodies fulfilling these responsibilities (except for Racing Victoria Limited), with only Queensland and Tasmania having an authority sitting over and representing the 3 racing codes as RWWA does currently. This integration would appear to have in overall terms served the WA racing industry well. However, these governance issues are not a specific focus of this Report.

6.2 Considerations for Privatising WATAB

As the WATAB does not separately exist and is essentially a division of RWWA, there is currently no specific entity to sell. Accordingly, in talking about privatising the WATAB, the Government would appear to be referring to having a private sector entity operating the wagering responsibilities that currently sit in RWWA.

So the WA Government, if it is to privatise the WATAB, will need to put in place the following in whatever forms that they may determine (some of which currently exist within RWWA):

- A wagering licence and/or wagering operator's licence for a term to be determined that authorises the wagering operator to conduct exclusive retail tote and fixed odds wagering and perhaps other products under certain conditions and requirements, and contains the Racing Industry funding obligations, (no such formal licence currently exists as RWWA's wagering authorities sit within its own Act).
- The WA Racing Industry Funding Model under which WATAB funds the WA Racing Industry so that the Industry is at the least no worse off.
- The legislative framework under which this new model will operate
- The legal structure under which the wagering operator is to operate – whether it is required to enter into a form of joint venture with the WA Racing Industry or stand alone with or without industry funding arrangements
- A Racing Program Agreement under which the wagering operator and the WA Racing Industry determine the annual racing program for the State.
- A Wagering Tax
- Racefield Fee flows and arrangements for the wagering operator
- Arrangements for various financial elements including GST reimbursement, unclaimed dividends, fractions and other subsidies
- Pooling arrangements, if required
- Arrangements with TAB retail outlets
- Arrangements with Racing Clubs for on-course wagering

In addition to establishing these arrangements for the wagering operator, the WA Government will also need to consider the following:

- As discussed earlier, the governance structure for PRA responsibilities including racing integrity and operations, and for wagering integrity, under the new arrangements flowing from the matters outlined above.
- Staffing arrangements for RWWA's wagering staff
- Arrangements in relation to the wagering related assets of RWWA such as the wagering systems, the telecommunications infrastructure, retail information technology, data centres, office accommodation, etc.

These matters will now be discussed in some detail noting the implications for the WA Racing Industry, the wagering operator, and the WA Government where appropriate.

6.2.1. **WATAB Privatised Model Features**

The following elements of a privatised wagering model would all need to be established for the potential privatisation of WATAB but will differ in form depending upon the structure decisions taken by the WA Government in the process.

6.2.1.1 **The Wagering Licence**

Pursuant to the relevant enabling legislation (to be discussed below), in a privatised TAB model the WA Government will issue a wagering licence to the new operator authorising them to conduct the wagering activities as defined lawfully in the State and elsewhere. As previously discussed such a licence does not currently exist, and hence in a potential privatisation of WATAB a new licence will be issued to a new operator. Whilst legal advice would need to be sought to confirm the following it is believed that in this case the Australian Competition and Consumer Commission may not have an involvement as the issuing of new gambling licences could appear to fall outside of its jurisdiction (but this would need to be checked). The major considerations in such a licence (but clearly not an exhaustive list) are:

(a) The Term of the Wagering Licence

The term or length of the wagering licence is a critical factor in establishing the certainty for the wagering operator of their tenure and the length of time guaranteed to them to recoup their investment. The approach between States does vary in this respect, with the Victorian Government in recent times having a preference for relatively shorter term gambling licences, seemingly to enable them to regularly bring the licences to a competitive market bid process and to raise money through up-front licence payments on a regular basis. Others such as the Queensland Government has issued the wagering licence out to 2098, Tasmania's licence acquired by Tatts Group in 2012 was for 50 years with a 49 year option, and the recent purchase of ACTTAB by Tabcorp came with a 50 year licence.

With the continually changing landscape of wagering in Australia, the potential impacts of this on the positioning and performance of TAB's, and the interaction of exclusivity and racing industry funding arrangements within the licence, if a longer term is adopted it is important that review points exist throughout the licence. This is particularly so in relation to racing industry funding to be discussed below.

(b) Exclusivity

WATAB/RWWA currently has the exclusive rights to provide retail tote and fixed odds wagering in WA, as it is the only wagering operator authorised to do so. Digital and mobile wagering clearly cannot be exclusively licenced by its very nature.

Section 3.1.3 of this Report explains the fundamental position of such exclusivity with a TAB wagering licence, both in respect to the value of the exclusive licence providing the security of sole retail access to Western Australian punters, as well as the inter-related obligations to fund the WA Racing Industry having received such a valuable licence. Within Western Australia this value is enhanced compared to other Australian jurisdictions given the absence of keno and electronic gaming machines offers being available outside of the Crown Casino at Burswood. This exclusivity provision will manifest itself as a positive undertaking by the WA Government that it will not issue another retail wagering licence. This is the case (in slightly different ways) in all States and Territories around Australia.

Shorter licence terms tend to be accompanied by such exclusivity for the same time period. Some of the longer term licences have shorter periods providing such exclusivity to give the relevant Government the opportunity for a review point at which to consider whether another licence provider might be appropriately introduced at a point in the future, and/or to restructure elements of the existing licence in any extension of the exclusivity.

An example of this was that Tatts Group's exclusivity ran to June 2014 in Queensland even though its licence runs to 2098. In the middle of this year after a Government review of the arrangements, Tatts' exclusivity was extended for 30 years to 2044, with a number of adjustments to its licence, including substantive adjustments to financial arrangements. Exclusivity in NSW was extended for 20 years in June 2013 for the up-front payment of $75 million as another example of this – the licence was issued in 1998 for 99 years. In the more recent privatisation of the Tasmanian TAB the licence was for 50 years with a 49 year option, but exclusivity was provided for just 15 years.

If the WA Government adopts a long term licence a shorter term exclusivity provision establishes a useful review point of the licence.

(c) Products and Channels

The WA Government has an opportunity to look at the extent of the products coverage that a new wagering licence could encompass. Clearly the licence will cover pari-mutuel (totalisator) betting on racing and sport and fixed odds wagering on racing and sport, replicating the current WATAB/RWWA product set.

In some other jurisdictions the retail product offer in TAB's has been expanded to include a simulated racing event product or virtual racing, commonly known as Trackside in Australia, offering effectively fixed odds using simulated racing animals. Statewide linked keno product has been allowed in certain jurisdictions. It is understood that RWWA has been unsuccessful to date in its attempts to obtain WA Government approval for such products.

The WA Government could receive increased up-front payments and on-going gambling tax proceeds from such product extensions. If these were included in the wagering licence then the racing (and sport) industries should also have access to appropriate shares of the returns to these products, as they would sit in the retail TAB outlets alongside the wagering product. Such products are currently operating in Crown's Burswood Casino and hence how such arrangements could be considered are not clear. Virtual racing is a product that the WA Racing Industry should seek the WA Government to consider within the wagering licence to enhance the overall Racing Industry funding model.

6.2.1.2 **The Legislative Framework**

The current legislative framework under which the WATAB operates at present was outlined in Section 3.1. The WA Government will need to review this framework if a privatisation is to occur to take the wagering responsibilities out of the RWWA Act and to establish the basis for creating and granting a licence and implementing the considerations outlined in this Chapter of this Report. Whilst much of these amendments will be mechanical in the sense of dealing with the technical amendments needed to deal with the move from public to private operation of the TAB functions, other considerations that will be important to the wagering operator and to the WA Racing Industry in the context of the performance of (and therefore funding from) the wagering operator are:

- The need to provide a regulatory regime that reflects similar attributes to those currently faced by the new wagering operator if the operator operates in other jurisdictions to ensure effectiveness of the integration of the WATAB betting turnover into the buyer's existing pool.
- Even if the buyer does not have an existing pool, it will nevertheless be necessary to provide more flexibility and more timeliness and formality of process in decision processes around regulatory approvals than currently exists in the present regulatory regime, particularly in terms of Government approval timefames.
- In this context the wagering operator will obviously need to comply with wagering regulation and appropriate financial reporting for wagering tax and pari-mutuel minimum return to player requirements, but should otherwise be free to conduct their business within necessary integrity requirements and approved broad product parameters without reference to WA Government. Agreed decision-making processes and timings on new betting products should be established to ensure timely decisions in the fast moving wagering industry.

The current regime under which RWWA operates is simply not efficient nor flexible enough to meet these requirements and requires significant streamlining. This has in part been either an excuse or a reason for RWWA's lagged developments into the modern wagering space in terms of retail information systems, digital and mobile, a competitive fixed odds offer, and in terms of a broader product offer which today has improved significantly but later than the rest of the wagering market. Improvements here will benefit the returns of the wagering operator, adding value to the WATAB and also to the returns to the WA Racing Industry.

6.2.1.3 **Structure / Models**

If the WA Government does proceed with the privatisation of the TAB, the WA Government will need to determine the structure or model within which it wishes the new wagering operator to work. Whilst in limited instances of privatisations of gambling assets the bidders have been able to bid a structure into the competitive sale process this is not the normal approach. It is critical for the WA racing industry that if privatisation is to occur that the Industry has had the opportunity to engage with the WA Government prior to the process of sale commencing to have determined with the Government the structure and model under which wagering is to operate going forward.

What Could Privatisation Of WATAB Look Like?

As outlined in Section 3.2.4 there are essentially three models operating elsewhere in Australia that can generally be identified as:

- The joint venture model – typified by significant joint decision-making and a profit-share arrangement after appropriate funding directions are satisfied (Victoria / New South Wales)
- The contractual model – the wagering operator and the racing industry have contracts in place on funding and racing program determination processes but otherwise separately pursue their respective responsibilities (Queensland / South Australia).
- The separation model – no formal relationship between the wagering operator and the racing industry, with the industry funded directly by the relevant State / Territory Government (ACT / Northern Territory)

There is one further model that in essence reflects the RWWA model but in private hands, and that is where the Racing Industry owns and operates the wagering operator. This obviously requires the Racing Industry to have the governance and corporate structures to privately run racing and wagering. This would require a structure such as that of Racing Victoria Limited, which itself could arguably consider obtaining a wagering licence given its ownership and corporate structure. Some of the internal governance issues and strategic and operational priority decision-making difficulties with this model were discussed earlier in Section 6.1.

The pros and cons of each of these structural options, with an eye to the implications for the WA Racing Industry in any potential privatisation of WATAB, are set out in Table 6.2.1.3.

TABLE 6.2.1.3 STRUCTURAL OPTIONS

STRUCTURE	PROS	CONS
1. Joint Venture Model - Racing Industry Funding under JV Agreement • Share of Revenue • Fixed product payment streams • Share of Profit - Covers 3 codes - Approval rights over material contracts - Sole licensee - Licence condition to enter into JV - JV Management Committee (Board) and JV Operations Committee - Wagering Tax	• Opportunity for better alignment between wagering operator and WA Racing • Racing Industry has seat at table of significant funder of the industry • Government incentivised to support both parties	• Each Party has competing requirements so alignment on key issues difficult • Inefficient decision-making through Committee structures • Neither party really satisfied with outcomes or with its operation
2. Contractual Model - Racing Industry Funding under Agreement between wagering operator and Racing • Share of Revenue • Fixed payment streams - Sole licensee - Racing Program Agreement requiring parties to agree racing requirements - Wagering Tax - Covers 3 codes	• Funding arrangements and racing issue interactions contracted and clear • Outside these arrangements parties free to pursue their respective agendas	• Racing Industry has effectively no input to the wagering operators business • Risk that wagering operator may not maximise local wagering if more profitable external opportunities • Less alignment between the two parties • Funding structure levels must be set at appropriate levels because almost totally revenue level dependent on wagering operator's performance
3. Separation Model • Racing Industry funding entirely from Government • Sole licensee • Limited wagering tax / Licence Fee	• Highest payment to Government by buyer	• No relationship or control by racing industry of wagering operator – no alignment • Racing Industry funding subject to annual Government budget pressures and decisions • 3 codes deal with Government
4. Racing Industry Ownership of Wagering Operator - Racing Industry funding all internally generated and managed - Sole licensee - Wagering Tax	• Issues of funding, etc all determined by the industry • Racing Industry separate from Government except for tax and compliance	• Limited capacity for upfront payment to Government because retain wagering infrastructure • Questionable ability to manage inherent conflicts between racing and wagering • Highly dependent upon wagering success

The separation model is one that should be avoided for Western Australia given the size and importance of the WA Racing Industry to the State and its ability to largely self-fund it operations with appropriate WATAB funding. The WA Racing Industry must avoid a model where it totally relies on the WA Government for its funding. One of the stated reasons for the establishment of RWWA and integration of the TAB into RWWA was to separate the racing clubs from the WA Government in terms of direct advocacy. This would be totally reversed by the separation model which would force the WA Racing Industry to actively engage with the WA Government. Even if commitments where made to the WA Racing Industry by the WA Government, the inability to bind future Governments and changing political priorities would clearly put strong doubt on the sustainability of any such commitments.

Racing Industry ownership and operation of the wagering operator in Western Australia is an interesting but highly questionable option. In a governance sense this would be effectively reversing the Principal Racing Authority vesting in RWWA by establishing an entity owned by the Codes (through taking RWWA out of a statutory body environment) that took back these responsibilities. The WA racing industry, as discussed in Section 6.1, generally supported the PRA process due to its improved governance framework to that previously operating under Code specific PRA's, and hence it is difficult to see the benefit in reversion, particularly in a private sector operation.

Whilst the size, the cross-checking balances of the various stakeholders in the Victorian market, and the significant funding and operational independence of the industry with its own wagering pool and the sustaining Spring Carnival, of the Victorian Racing Industry could arguable support such a Victoria TAB ownership model by the Racing Industry, the Western Australian Racing Industry is extremely unlikely to be able to create and sustain such a model. The issues between Codes prior to the creation of RWWA would suggest difficulty with this model. In addition, an industry-owned wagering operator would need to retain all the existing infrastructure of WATAB and its pooling dependencies, so any privatisation sale to the WA Racing Industry would probably realise less in up front payment to the WA Government than if sold to an existing TAB operator if it was to be a viable proposition for the WA Racing Industry. Given just these two propositions, this model is not a recommended course of action to be pursued by the WA Racing Industry.

At this stage of the WA Government's process as it is currently understood, where there appears to have been limited detailed consideration of such issues, a specific recommendation on a preferred structure from the joint venture and contractual models is premature. This will be more informed and determined by decisions on the financial and industry funding models, by the licencing and legislative structures to be instituted, and from the WA Racing Industry's engagement with the WA Government as to the objectives of any possible privatisation.

There is much to be said for the contracted model that requires and calls forward many decisions to be made up front in the sale process to enable the racing industry and wagering operator to enter contracts at the time of sale and then fulfil their respective responsibilities going forward. However, if these settings are not established with appropriate levels and coverage they can result in undesirable outcomes for all parties.

Having said that, any joint venture structure will require much of the same work to be done upfront, with this structure placing the racing industry even closer to the wagering operator and with a different risk profile because funding is usually dependent not just on revenue but both revenue and profits. It also establishes more decision-making infrastructure than the contractual model. This therefore is closer to the current RWWA/ WATAB model and hence may be a more appropriate transition. This is particularly so given these structures usually have "best interests" requirements that require the wagering operator to make decisions that do not disadvantage the local racing industry, an important requirement if proper alignment is to occur. Such alignment is critical to making a joint venture work appropriately. Such a provision is more easily monitored in a joint venture type structure than simply an arms-length contractual arrangement.

6.2.1.4 **Racing Industry Funding Model**

This Report has explained in some detail the current levels and nature of distributions and subsidies and other funding made by RWWA to the WA Racing Industry and the performance in this regard over recent years, as best it could determine (but total actual funding levels would need to be accurately determined in any potential WATAB privatisation).

Chapter 5 explained, again in significant detail, how these levels of distributions and overall funding by WATAB/RWWA are now calibrated to ensure stakes prizemoney levels are sufficient to continue to attract investment by owners to provide ongoing operational sustainability of the WA Racing Industry.

Accordingly, if a privatisation of the WATAB is to occur, the funding provided by the new wagering operator by way of product fee payments (reflecting distributions and subsidies) need to equal current levels of such RWWA distributions, subsidies and other payments and then continue to grow into the future to sustain the Racing Industry in Western Australia.

As the level and allocation of distributions by RWWA have been determined in-house with final decisions on these taken by the RWWA Board, the actual distribution policy and basis is not clear. However, in discussions with the Management of RWWA, the distributions are reviewed and established annually based around Board approved key principles that are understood to reflect some of the matters as outlined in Section 5.2.2.2.

It would appear however, that there is no specific targeting of a percentage of revenue or profit of WATAB/RWWA from such an approach, but rather a determination of levels that will ensure ongoing viability of the WA Racing Industry. In recent years as discussed earlier, the strong turnover and revenue growth together with reduced pooling fee costs, have enabled RWWA to also put aside cash reserves to assist in smoothing and supporting (if necessary) distributions into the future.

Looking at the period from 2008/9 to 2012/13 from RWWA Annual Report data (which includes sports wagering turnover and sport distributions), this is reflected by the following numbers:

- Wagering turnover grew by 28% or around 6.3% per annum
- Wagering margin grew by 25.5% or around 5.8% per annum
- Distributions grew by only 6.8% or 1.7% per annum
- Distributions as a percentage of margin in each year were:

2008/9	40.33%
2009/10	39.31%
2010/11	37.27%
2011/12	35.65%
2012/13	34.34%

Section 5.2.2.3 of this Report showed however that going back 8 years dramatically changed these figures, especially distribution growth rates. As discussed, with the impacts of equine influenza and changed pooling fees, the 2008/9 year reflected a loss of around $13 million (excluding grants) after distributions had been increased despite the profit deterioration, and then the decrease in distributions in 2009/10 as the flow on result. The figures as outlined above then show the slowdown in the growth of distributions despite wagering turnover and margin growth as cash has been reserved to provide future protection for similar such events or impacts. Accordingly, any consideration of funding arrangements for the WA Racing Industry under a potential privatisation needs to consider these trends and RWWA management decisions closely.

In a more conceptual sense, in establishing the WA Racing Industry funding model in a potential WATAB privatisation, consideration also needs to be given to whether simply a margin percentage share or a combination of margin and profit share is a more appropriate model. In a comparison sense around risk profile and return to the current RWWA model, it would be contended that the current WATAB/RWWA model and distribution policy reflects a margin and profit share model, or even perhaps a profit share model when other payments and subsidies are included.

Whilst distribution levels have been based on meeting key operational and strategic objectives including stakes prizemoney levels and appropriate national relativities of these, it would appear that the ultimate level of distributions has been finally determined on profitability and reserving considerations. This perspective of profit rather than margin focus to funding the WA Racing Industry is further reinforced by the situation that pooling fees and costs associated with the premium market (particularly international players) are not in the margin calculation but in the cost of sales deducted from that margin.

Whilst most if not all of these features may not exist under a privatised model, the WA Racing Industry cannot form a view on these matters at this time until all aspects of the proposed privatisation are put together, although total reliance on profit share is not recommended as an option.

It must be understood that any racing industry funding arrangement that is based on a share of turnover, margin or revenue puts the WA Racing Industry in a position of relying on the performance of the wagering operator. This is in effect no different from the current situation with WATAB/RWWA as has been discussed throughout this Report, however the management and governance structures will be separate and different in a privatised WATAB environment. Subject to differences in perspective, it does align the financial interests of the racing industry and wagering operator, with this alignment even greater under a share of profit model.

Share of revenue or margin will provide diversification of revenue across all racing and wagering jurisdictions and Codes, and potentially across sport (depending upon the arrangements put in place), as well as perhaps new products such as virtual racing as a growth option in the retail wagering outlets. Again, the critical issues here if privatisation was to occur is to ensure any structure establishes an appropriate share allocation up front to support the required WA Racing Industry funding model, that there is a potential to review this if funding falls away, and that the wagering operator ensures maintenance and growth of the turnover streams of the WATAB (or that there are adjustment factors and other mechanisms built into the structure to protect the WA Racing Industry).

A share of the wagering operators profit will usually reflect more of a joint venture type structure with involvement of both parties in elements of strategic and operational decision-making relating to relevant racing and wagering issues (which can be a divisive and inefficient process over time). The racing industry's financial position therefore becomes exposed to the cost performance of the wagering operator, including issues around how costs may be allocated by the wagering operator across various jurisdictions if it operates wagering activities in other locations. In addition, a matter of significant difficulty and debate is always the definition of profit, with questions over revenue attribution, cost allocation, and the application of various accounting policies.

In addition to this question of margin/revenue share or profit and margin share, there are a number of other prospective aspects that need to be considered :

- In any prospective product fee structure there should be an element of fixed payment to reduce the risk profile associated with the wagering operator's performance.
- A minimum racing industry funding obligation on the wagering operator for a period of up to 5 years to ensure any privatisation does not diminish the current expected funding in the absence of privatisation for that period (ie, continuity of the current model).
- If privatisation occurs, "Racing Western Australia" being obliged to maintain its cash reserves for the purposes of longer term distribution stability and/or infrastructure funding.
- Inclusion of specific requirements around stakes prizemoney levels and infrastructure funding requirements in any structure as part of the minimum performance/funding obligations required under a privatised model.
- The need to ensure that the administration and integrity requirements of the Racing Operations activities are fully funded.

In considering this WA Racing Industry Funding Model in a potential privatisation of WATAB it is necessary that the levels set within the Funding Model cover all forms of funding provided to the WA Racing Industry by WATAB/RWWA. This Report has discussed many of these funding flows to the WA Racing Industry which include the following (although this list may not be exhaustive):

- Stakes prizemoney funding
- Event fee payments to Racing Clubs
- Training funding to Racing Clubs and RWWA training facilities
- Jockeys and Drivers payments
- Breeders and Owners Bonus/Incentive Schemes
- Product fees, broadcast costs and other payments on behalf of Racing Clubs
- Cost of RWWA's Racing Operations Groups

Attempting to establish how such a funding position for the WA Racing Industry compares to the relative levels provided to racing industries in other Australian jurisdictions is difficult given the different reporting styles and classifications of such funding used across these jurisdictions. At a general level some analysis was attempted to express Racing Industry funding as a percentage of the TAB racing wagering turnover within each jurisdiction. Given the difficulties of determining the total funding figure for the reasons stated above, the following broad but largely unsubstantiated observations are made from this analysis :

- The Western Australian Racing Industry would seem to be around broadly similar levels as Victoria at the upper end of funding proportion at approximately 7.5% of TAB racing wagering turnover
- New South Wales and Queensland would appear to be around approximately 5.0% of TAB racing wagering turnover, although Queensland probably jumped to over 5.5% with increased funding in 2012/13
- It would appear that South Australia would be much closer to Victoria and Western Australia than to New South Wales or Queensland, following the abolition of wagering tax payments in South Australia.

The discussions in Section 5.3 of this Report in relation to the value chains of each Code in the WA Racing Industry reflect the high cost nature of producing the racing product within Western Australia. With the vast size of the State adding to the costs of presenting the product, combined with the essentially isolated self-funding nature of Western Australian racing relative to the Eastern States industries, such funding levels are both understandable and justified. The more recent increases in funding for South Australia (through the wagering tax abolition), and for Queensland in the recent amendments to the financial arrangements for the wagering licence, reflect recognition of the need for the types of Racing Industry funding levels existing in Victoria and Western Australia.

6.2.1.5 Racing Program Agreement

At present RWWA makes decisions, after input from Racing Clubs and Code Consultative Groups, as to the Annual Racing Program for the entire Western Australian racing industry. After such consultation/input the RWWA Management team and ultimately the RWWA Board decide the program internally as part of their Budget process. This arises out of the Racing and Wagering Management making the competing calls along with the agreement of Senior Management, and then the Board, (with its Code representatives), contributing and ultimately deciding the acceptable comprises between racing and wagering objectives in the racing program determined. In a privatised TAB model this needs to become a negotiation between two separate entities – the wagering operator and the racing industry – one looking to maximise wagering turnover for profit purposes and the other looking to fund and sustain a whole State's racing industry with appropriate integrity, regional, social, employment and industry sustainability objectives being met.

In a privatised model therefore it is necessary to have a formal agreement / contract / resolution methodology that is a condition of the licence, between the wagering operator and the racing industry, that sets out how the racing program and various related matters are to be negotiated and resolved. In a contractual model this will take the form of a contract between the two parties, whilst if some form of joint venture is established it will form part of the matters outlined in a formal joint venture agreement between the parties.

Given the importance of this to the WA Racing Industry it is vitally important that in the event of the WATAB being privatised that the governance and representative structures for the WA Racing Industry are established appropriately to ensure all stakeholders are properly represented in such negotiations. A Racing Western Australia structure reflecting RWWA without wagering would seem best placed to provide the entity that is the party to this Agreement, subject to any improvements in this structure that participants deem necessary. With the removal of wagering under a privatised model it would be appropriate to review key objectives of the new entity, and the relevant skill set requirements of the Board and senior management called forward by these objectives, as well as the legal structure of the entity, to ensure appropriate focus to the racing product mandate of the new entity.

6.2.1.6 Wagering Tax

Wagering taxation is paid by WATAB/RWWA to the WA State Government on both pari-mutuel and fixed odds wagering. The tax rate on pari-mutuel betting is 11.91% on gross margin for racing, and 5.0% of turnover on pari-mutuel sport, whilst for fixed odds betting the wagering tax is based on turnover – 2.00% for racing and 0.50% for sport.

Such taxation represents an outflow that reduces the net earnings of the wagering operation and hence the amounts that could flow to the WA Racing Industry. It is nevertheless a payment to the WA Government in recognition of it granting a licence to the wagering operator, in addition to any upfront payment made to secure the licence. Where such wagering taxes are in place they are generally expressed as a percentage of revenue/margin in relation to pari-mutuel betting, and as a percentage of either revenue/margin or turnover in the case of fixed odds betting. In Tasmania and the ACT, where their TAB's have been recently privatised and the Government has taken over funding the racing industry, a fixed amount (escalated by CPI) is paid as a wagering levy by the wagering operator to the Government, but no wagering tax is in place.

Wagering taxes currently in place around Australia are set out in Table 6.2.1.6 over the page.

In recent times the trend by State Governments in Australia has been to reduce the levels of wagering taxation on the TAB wagering operators in recognition of the relatively higher product fees paid to local racing industries by the TAB compared to the racefield fees paid by all wagering operators, and to enhance funding to the Racing Industry by not taking the extent of wagering taxes out of the TAB. This is specifically the case with the corporate bookmakers competing with these TAB's who are based in low/no tax and/or fee jurisdictions such as the Northern Territory.

A very recent example of this tax reduction approach by State Governments was in the new framework for race and sports wagering for the TAB operated by Tatts Group in Queensland announced in June this year. The Queensland Government made a number of changes to these arrangements, including agreeing to a reduction in its pari-mutuel tax rate from 20% to 14% of commission (margin) and from 20% to 10% for fixed odds wagering.

Other examples of reductions in wagering taxes and/or other funding concessions by Australian State Governments post privatisation of their TAB are:

- In South Australia the Government removed the wagering tax in 2012 to improve racing industry funding, having phased is down from 2009;
- In Victoria the new licence and funding arrangements that commenced in 2012 included a reduction in wagering taxes;
- It is understood that in NSW consideration is being given to a reduction in the wagering tax rates to match the Victorian rates on pari-mutuel and fixed odds betting; and
- In a number of jurisdictions State Governments have expanded the wagering product definition to include products such as simulated racing events (eg, Trackside) to provide increased racing industry funding.

Given the participant financial situations within the WA Racing Industry as explained throughout this Report, there is clearly no room to increase the current wagering tax level and settings without significantly impacting the current industry situation. This is the case, in fact, whether privatisation was to occur or not, but clearly is also an important factor for the WA Government in overall value terms in any potential privatisation process. Having said that, and whilst a wagering tax rate reduction would increase the up-front payment offer from a potential bidder, the different costs of capital between the WA Government and a corporate bidder, could result in the bidder

TABLE 6.2.1.6 AUSTRALIAN OFF-COURSE TOTALISATOR TAX RATES

NSW	VIC	QLD	WA	SA	TAS	NT	ACT
Parimutuel Tax Rate 19.11% of player loss (i.e. gross deduction) A rebate of 9.11% in respect of investments made by international account holders (no minimum investment) and domestic account customers who wager more than $3m in totalisators per financial year Totalisator Sports Betting (FootyTAB, SoccerTAB, SportsTAB) Tax Rate 19.11% of player loss Fixed Odds Sports Betting **TAB Tax Rate:** 10.91% of gross margin	Parimutuel Tax Rate under the new wagering and betting licence, from 16 August 2012: 7.6% of player loss. The difference between pari-mutuel tax the licensee would have paid under the former tax framework, and tax payable under the new framework, is paid to the Victorian Racing Industry as a condition of the new licence. Totalisator Sports Betting Tax Rate 7.6% of player loss Fixed Odds Sports Betting **Tax Rate:** 4.38% of player loss Simulated Racing ('Trackside") **Tax Rate** 10.91% of player loss	14% of commission (gross deduction). Tax is collected monthly in arrears. GST credit provided. Fixed Odds Racing and Sport 10% of gross revenue (player loss)	**Racing** 11.91% of net of GST gross margin for off-course racing totalisator wagering (equivalent to a tax rate of around 3.50% on turnover). A rebate of 10.0% in respect of investments made by premium players. Fixed odds racing wagering 2% of turnover. **Sports** Pari-mutuel sports betting tax is set at 5% of turnover. Fixed odds sports betting is set at 0.50% of turnover. In addition, 20.5% (decreased from 25% from 1 August 2013 until 30 July 2015) of net return after tax is remitted to the Sports Wagering Account for disbursement by the Gaming and Wagering Commission on the direction of the Minister for Sport and Recreation. Sportsbetting Pari-mutuel 5% of turnover Fixed Odds: 0.5% of turnover	Wagering tax on SATAB race betting operations abolished from 1 July 2012. Wagering tax on non-race betting operations continues to apply; equivalent to a flat component of $252,500 per month and 6% of all net betting revenue other than net betting revenue attributable to Racing. Sports Betting and other non-racing betting SATAB will continue to pay a wagering tax equivalent to a flat component of $252,500 per month and 6% of all nett betting revenue attributable to Racing. This includes Sports Betting.	From 1 July 2009 Totalisator Wagering Levy of 4.7m fee units in 2013/14 this equates to $6,862,000	Totalisator 40% of licensee's commission deducted less GST. For races other than thoroughbred, harness horse and greyhound races and prescribed sporting events held: **In Australia:** 20% of licensee's commission deducted less GST. **Outside Australia:** 10% of licensee's commission deducted less GST	TAB Annual licence fee of $1 million indexed annually.

ascribing relatively less value to this reduction than the value of the ongoing stream at the WA Government's cost of capital.

However, a reduction in the wagering tax would improve the earnings available for funding of the WA Racing Industry.

6.2.1.7 Racefield Fees

The current arrangements with racefield fees in Western Australia are such that RWWA pay the racefield fees for interstate and international product for WATAB and on behalf of the Racing Clubs and, as explained in Section 3.1.4.5, receive racefield fees paid by wagering operators for the use of WA racing product via the Gaming and Wagering Commission. The Gaming and Wagering Commission receive these racefield fees and pass them on to RWWA (net of administration costs) to hide the source of fees from WATAB given the potential benefits of WATAB being aware of other wagering operators use of WA product.

It is understood that these figures are broadly equivalent, with a small positive balance forming part of the funding for the distributions to the WA Racing Industry.

In a privatised model such a structure would need to be examined given the separation of the wagering activity from racing product oversight which currently both reside in RWWA. Whilst in all jurisdictions, either directly or via Government the racefield fee receipts flow to the racing industry, the position with racefield fee payments out of the jurisdiction vary. In NSW they are paid by the wagering operator, in Victoria by the joint venture (and therefore shared 50/50 by the wagering operator and the racing industry), whilst in Queensland it is effectively the racing industry that meets the cost through an offset against the product fee paid to the racing industry under the RDA (subject to an adjustment to be shared 60% Tatts / 40% Racing Queensland if outflows exceed inflows).

In the case of Western Australia as outlined above, RWWA receives these racefield fees paid on WA racing and RWWA (probably more so WATAB) pays the racefield fees to other jurisdictions (although this also includes the Racing Clubs fees). Without the separation of the wagering activities in RWWA from the racing industry activities the issue of the financial balance responsibility and benefit associated with these racefield fee flows has not needed to be addressed.

Such attribution will, as in other jurisdictions as outlined above, need to be determined as part of the overall arrangements of a potential privatisation of WATAB, and will form an element of the financial machinations in such a privatisation. Clearly a NSW-type model would benefit the WA racing industry (industry receives incoming product fees whilst the wagering operator pays product fees to other jurisdictions), and it could be argued literally to be the current case. However, for the WA Racing Industry to be left in the same situation a model such as that in Queensland, but with the wagering operator however responsible for 100%, not 60%, of the shortfall, ie, where outflows exceeds inflows, would be an appropriate structure in a potential privatised model (again subject to all other things being equal).

6.2.1.8 Other Financial Arrangements

There are a variety of other fund flows and arrangements that are in place currently that need to be clarified under a privatisation model if it was to occur. From the WA Racing Industry's perspective it is necessary that these existing arrangements be retained within a privatisation model, but with some clarification to ensure the WA Racing Industry funding is protected in certain instances.

(a) GST Reimbursement

As was explained earlier when GST was introduced into Australia in 2000 there was no ability to change the "pricing" of wagering for this impost, so State Governments reimbursed wagering operators for the GST liability they were unable to pass on, from their global GST arrangements with the Federal Government, either through wagering tax adjustments or direct reimbursement (the WA Government originally adopted the latter method). Subsequently the WA Government adjusted down the racing wagering tax rates to replace the need for reimbursement, but such reimbursement remains for fixed odds and pari-mutuel sport. It may be appropriate in a new licence regime if privatisation is to occur to adjust tax rates for these items to avoid the need for a reimbursement process. This issue clearly sits with the potential new wagering operator and the WA Government in a privatisation process.

(b) Unclaimed Dividends

As explained in Section 3.1.4.5 unclaimed dividends on racing wagering (after 7 months) became the funds of RWWA, whilst on sports they flow to the Sports Wagering Account held by the Gaming and Wagering Commission. This important source of funding for the distributions and other payments made to the WA Racing Industry by RWWA needs to be retained by the WA Racing Industry, and hence in any privatised model the unclaimed dividends should be paid through directly to the Racing Industry (Racing Western Australia) by the wagering operator after the 7 month period. The treatment of unclaimed dividends on sports wagering should remain as it currently operates.

(c) Fractions

Given the mechanics of these and how they arise it would seem appropriate that these stay with the wagering operator in any potential WATAB privatisation as they are an inherent part of the wagering operation. Given that these represent around 0.4% of margin annually it is however necessary that in any product fee rate determination based on margin as part of the privatisation structure, appropriate recognition be given to this matter.

(d) Premium Market Rebates

Whilst this customer segment may not be one that buyers will value nor seek to continue with a WA operation, if it is then existing rebates through different wagering tax rates will need to be considered in any privatisation process. If these are to continue then this will need to form part of the licence entered into by the new wagering operator. If these fall away and/or the premium customer base does not continue post privatisation, racing industry funding models based on percentages of margin, revenue or turnover will need to reflect this if funding levels to the WA Racing Industry are to be maintained.

6.2.1.9 **Pooling Arrangements (if required)**

As explained in Section 3.1.4.3, WATAB/RWWA has entered into a pooling agreement with Tabcorp's Victorian based SuperTAB pool, under which nearly all WATAB tote bets are pooled in with the SuperTAB pool. As also explained earlier, WATAB/RWWA has a management agreement with William Hill under which WATAB's fixed odds pool is managed by William Hill for a fee.

In a privatisation process, the value and situation with each of these will vary depending upon the situation of the potential bidder. If Tabcorp or Tatts Group are bidders, they both obviously already have their own pools and wagering (tote and fixed odds) capabilities that means that WATAB/RWWA's existing pooling arrangements will no longer be required. If a bidder is an existing corporate bookmaker with existing fixed odds wagering capability, the Tabcorp pooling agreement could probably be required to continue but not the William Hill arrangement.

Although less likely to occur, a bidder with no existing wagering capabilities would clearly most probably wish to retain such arrangements. It is understood from discussions with RWWA management, which would be expected, that these agreements have payout arrangements associated with early termination. As it is understood that these are relatively long term agreements, such termination payments could be expected to be considerable and will be incurred by RWWA in a privatisation process if a new wagering operator does not require such arrangements.

In the case of Tabcorp it is unclear exactly what Tabcorp would choose to do with the existing Pooling Agreement given the Joint Venture with the Victorian Racing Industry in relation to the SuperTAB Pool. In the case of Tatts Group no such pooling arrangement with Tabcorp would be required. Given early termination provisions exist, it is expected that this would lead to some form of substantial payout being required to Tabcorp to terminate the contract which is understood to have some 9-10 years to run. Similarly, in any privatisation that led to the acquirer not requiring the fixed odds management services of William Hill, this contract would also need to be terminated and again a substantial payout would be expected to be required for such termination.

6.2.1.10 **WATAB Retail Outlet Arrangements**

WATAB/RWWA will have in place with the various hotels and retail outlets that have TAB operations a variety of contracts/agreements that provide varying degrees of goodwill value to these businesses. A new wagering operator would obviously look to maintain a retail network, but will seek to have some flexibility to operate it in a manner it wishes in terms of locations and "look and feel" that may or may not be reflected in the current WATAB/RWWA network.

Retail outlets will, conversely, look for some certainty in their future arrangements under a new operator if privatisation is to occur. Such certainty will generally relate to financial arrangements and remuneration and to the length (timeframe) and terms of their agreements. In a number of similar privatisations such agreements under existing terms have been locked in for a fixed period (eg 3 or 5 years). The Government will need to determine this matter prior to any privatisation, as a bidder will more highly value some flexibility.

6.2.1.11 **On-Course Wagering Arrangements**

With Racing Clubs holding the on-course wagering licences in Western Australia, as is the case in other jurisdictions, it will be necessary in any potential privatisation to ensure appropriate arrangements and structures are put in place within the wagering licence to cater appropriately for the Racing Clubs and the wagering operator. As discussed in Section 5.2.3, a combination of outdated regulation, system deficiencies, competition, and prioritisation by RWWA to off-course wagering at the expense of on-course wagering, has seen on-course wagering decline substantially, together with falling attendances and underinvestment in Racing Club infrastructure.

As this area can be one of potential value enhancement for both the wagering operator and the Racing Clubs into the future, whether it is a privatised model or not, the current improved developments between RWWA and the Racing Clubs must be continued. In a potential privatisation it is absolutely necessary for these improvements to be a considered within a new licence. Accordingly, future on-course wagering under either a privatised or continuing model needs to include active consideration of:

- The ability for Racing Clubs to conduct fixed odds betting under their wagering licences, in addition to the pari-mutuel wagering as currently provided.
- Remove restrictions on the numbers of operator and self-service terminals on track
- Allow and require the wagering operator to provide the same racing information systems on-course as provided off-course.
- Require the wagering operator to enter into on-course wagering agreements with Clubs if requested on reasonable terms to both parties (as currently is the case)
- The wagering operator providing the ability for roaming TAB operators, and to be able to take verbal bets on-course using operators
- Centralised administration of the Australian Price Network for fixed odds pricing
- A requirement for the wagering operator to provide the technology to capture on-course mobile betting with the wagering operator, maintaining the on-course wagering tax exemptions.

6.2.1.12 **Racing Industry Governance Structure**

This issue has been discussed elsewhere in this Report. If privatisation does occur, as outlined earlier, an entity such a Racing Western Australia representing all Codes and all racing industry participants will need to be formed (or in the case of RWWA reformed) to provide the primary entity to represent the WA Racing Industry in joint venture/contractual or other arrangements with the wagering operator, and to oversee integrity and programming in the Western Australian racing industry.

6.2.1.13 **RWWA Staffing Arrangements**

If an existing TAB operator obtains the WATAB licence then it is highly likely that the bulk of the wagering operation will be run from their wagering head office operation interstate. If a non-TAB wagering operator was to be the successful party they would need to retain much of the WATAB operations.

So if an existing TAB operator is successful most of the people employed in the Marketing and Retail divisions would not be required, and many of the Information Services staff would probably not be required. A buyer may seek to retain some call centre staff if time zone differences are considered to be best managed by a local call centre. Some of the Retail Division would be retained to service the retail WATAB network. Most if not all of the shared service functions of Finance and Business Services and Human Resources that relate to wagering would not be required. Of course, depending upon WA Government decisions on the remaining structures for RWWA, such as a Racing Western Australia, much of the rest of RWWA's organisation chart, with substantially trimmed technology and shared services functions, could continue in this new framework.

In any potential privatisation a decision will need to be taken as to which parties are responsible for the people whose roles are to be lost, and how any particular transfers of roles from RWWA to a new wagering operator are to be effected.

As a significant part of any value to an existing TAB operator of the WATAB licence will be in the ability to extract cost synergies from its operation by effectively undertaking a number of existing roles from its own existing interstate staff, any obligations for non-required RWWA staff will reduce the value of the licence. The WA Government will therefore need to determine if it requires the new wagering operator to take over the employment contracts of all the wagering-related staff of RWWA and then leave it to the operator to make employment decisions and deal with the redundancy arrangements, or allows the operator to seek to retain only those employees it requires transferred to its employment upon privatisation occurring.

In the latter case, RWWA and/or the WA Government will need to deal with redundancy/ re-deployment arrangements as appropriate. The WA Government may require certain arrangements for transferring staff in terms of existing entitlements. In either case the WA Government will need to determine whether it gives any period of job security to employees through a requirement in the privatisation process, and at whose expense, but the new wagering operator will probably want to ensure some short term availability for integration purposes.

6.2.1.14 **RWWA Wagering Asset Infrastructure**

A new wagering operator in a potential privatisation of WATAB which is an existing TAB operator will need to consider whether there are any benefits in retaining and using any of the wagering infrastructure of WATAB/RWWA, or rolling out its own infrastructure.

The key assets in this regard are the betting engine system, the retail TAB outlet fit-outs and racewall information system, the telecommunications infrastructure in place to support the off-course and on-course betting, and the digital/mobile betting infrastructure of TABtouch. Whilst these are clearly decisions to be made at the appropriate time, it is anticipated that any such purchaser will look to generate savings and efficiencies from single technology platforms across its network and not duplicate such technology. Which elements it uses or discards in this process will be a corporate decision at the time, depending upon their existing scale and views on parts of RWWA's technology, particularly following recent investment by RWWA to enhance their wagering systems.

Any other non-TAB wagering operator who looks at the WATAB in a privatisation would most probably look to retain the existing infrastructure in the short/medium term

Whilst neither this nor the RWWA staffing arrangements directly impact the WA Racing Industry, they will determine the value that a potential privatisation may create in terms of up-front payment for the WA Government. This value equation may be critical in any final decision to privatise, and these matters therefore represent a key element of where a potential new wagering operator can look to quickly extract synergies from the integration of the WATAB operation into its existing business. This is where issues around the question of where the shareholders of a buyer will get benefit whilst maintaining existing other stakeholder flows will be partly answered. If a new operator can optimise these synergies and pay a reasonable price up front, then their shareholders can still benefit whilst the WA Racing Industry continues to receive its funding. But if the WA Government's up-front value expectations are too great and hence the sharing of these synergy benefits between Government and new wagering operator in this sale are too weighted to Government, pressure may fall on the WA Racing Industry funding to make up the shortfall if a privatisation was still to occur.

6.3 Funding and Sustainability of Racing in Western Australia

This section of this Report discusses the current and prospective future funding position and framework for racing in Western Australia, looking at these in the context of whether or not WATAB is privatised.

6.3.1 Background

This Report in a number of previous sections has outlined the significant role that the WA Racing Industry plays in the State of Western Australia. The Report has also outlined that the Western Australian racing product generates around a quarter of WATAB's wagering turnover and earnings, and would appear to generate around 8% of total wagering turnover Australia wide.

Accordingly, not only is the value and profitability of the WATAB/RWWA wagering business highly dependent upon the operation, sustainability and development of the Western Australian Racing Industry, but to varying degrees so are the operations of other State and Territory TAB's, and other wagering operators (bookmakers). So whilst the "gentlemen's agreement" of the past between TAB's no longer applies, the "balance" of the Australian industry continues to be maintained by the TAB's providing (in most cases) the sufficient funding to their local racing industry to ensure that their jurisdiction provides suitable racing product for themselves and other TAB's (and other wagering operators) to profitably undertake their wagering activities.

What Could Privatisation Of WATAB Look Like?

Chapter 5 of this Report outlined the importance of the racing industry distributions and other payments currently paid by RWWA and funded by the wagering activities of WATAB in ensuring that this is and continues to be the case in Western Australia. When provision of racing product by the Western Australia racing industry is discussed, the totality of this provision covers all of the following to ensure that wagering is occurring at good levels for punters :

- Racing product of good quality and field sizes that is underpinned by appropriate stakes prizemoney for racing industry participants to continue to attract and retain appropriate people in the industry
- Ensuring training facilities are available and affordable to support the participants in the generation of the racing product.
- Maintaining a high level of integrity for all racing and race meetings to provide confidence in, and compliance within, the conduct of the racing product.
- Ongoing development within racing clubs and other stakeholder groupings to administer the tracks and racing industry participants activities on them.
- Continual investment in infrastructure and facilities to improve the raceday experience for all racing industry participants and punters, and to ensure the safety and wellbeing of these people.

It is the totality of the provision of all of these services that is the total requirements of the WA Racing Industry in terms of financial and physical resources to meet all of these functions. These are therefore the core activities of RWWA which are funded by WATAB/RWWA's current wagering activities. In the 2012/13 year the funding and costs of these activities can be summarised as follows from the RWWA Annual Report 2013, as adjusted following discussions with RWWA management:

Racing Services Expenses		$ 20.1 million
Wagering Services Expenses		$ 86.7 million
Support Services unallocated		$ 21.3 million
Distributions –	racing industry	$113.7 million
	sports industry	$ 4.0 million
Grants and subsidies to racing industry		$ 2.2 million
		$248.0 million

Excluding the wagering services expenses and any component of the support services expenses relating to wagering, the remaining expenditures above (probably with some dis-synergy from extracting out the wagering business) would need to continue to be provided to the WA Racing Industry and its administration under a privatised model to ensure the quality of its product supports the Western Australian and Australian wagering businesses. Obviously the new wagering operator of a privatised WATAB would need to take on the funding responsibilities to the WA Racing Industry under its licence, and directly meet the costs of the wagering activities it would then be conducting. Therefore the WA Racing Industry funding obligations that would need to be put in place if WATAB is privatised will need to include mechanisms to ensure that all of these expenditure elements (excluding the wagering items) are fully funded now and into the future.

Clearly this is the case whether privatisation occurs or not, but obviously under a potential privatisation these would need to be more clearly and formally documented and contracted given the wagering operations would in that case be separated from the primary racing authority entity, and in private ownership. So it would need to be clearly documented that the race programming, promotion, racing integrity, stakeholder representation and infrastructure investment for the WA Racing Industry must be funded in addition to the distributions currently paid to racing clubs and to participants. From the table above this can be seen to cover the operational expenditures of RWWA's Racing Services, the relevant proportion of RWWA's shared services (including technology that support these Racing Services), various grants, subsidies and other payments provided to the WA Racing Industry by RWWA, and obviously then the distributions made by RWWA. In addition, a mechanism for funding racing industry infrastructure requirements would be required as discussed earlier in Section 5.2.4.

6.3.2 **Funding of the Industry from Wagering – Past and Future**

In sections 5.2.2 and 6.2.1.4 of this Report the distribution funding provided to the WA Racing Industry in the recent past has been discussed, together with potential models in a privatised model. This section will also look at what has been the growth of the other expenditure elements of RWWA that relate to its non-wagering function as outlined in the previous section.

On the basis of the past, and some assessment of WATAB/RWWA's positioning in the future Australian wagering market if it were not to be privatised, some future outlooks are considered to assess what could be a reasonable outlook for WA Racing Industry funding from wagering over the next five years.

6.3.2.1 **RWWA Cost Base**

As outlined in the previous section, under any privatisation model the funding from the new wagering operator to the WA racing industry would also need to include the expenditure of the "new" PRA entity to fulfil its various responsibilities undertaken on behalf of the WA Racing Industry as a whole, as well as all the funding to Racing Clubs and participants. Without being privy to all of the detailed financial numbers of RWWA, the following outline of expenditures of the organisation are taken from its Annual Reports.

Year	Racing Expenses ($M)	Wagering Expenses ($M)	Unallocated Expenses ($M)	Total Expenses ($M)
2007/08	15.392	68.388	26.188	109.918
2008/09	15.688	74.236	26.736	116.660
2009/10	13.247	76.081	26.956	116.284
2010/11	14.066	77.369	28.026	119.461
2011/12	14.848	80.536	30.236	125.620
2012/13	15.557	82.549	29.966	128.072

Whilst the 2012/13 figures do not line up with those in the previous section in terms of allocation of costs, the focus here is on the trends in these costs as classified in the accounts. The Racing Services expenditures show a steady increase of 17.44% since 2009/10 (or just under 4% per annum compounding) following the reduction in staff reflecting a similar response to the factors that led to reduced racing industry distributions in that year as explained previously in this Report. From 2007/08 wagering expenses, which would be met but differently managed by a new wagering operator after a potential privatisation as outlined earlier, had increased by 14.21% to 2012/13. For the same period, unallocated expenses increased by 14.43%, of which it is hypothesised that most of this increase would reflect wagering related expenditures in this category.

Accordingly, based on this high level analysis and subject to more due diligence being performed on these cost base expenditure numbers in any privatisation process, a funding model would need to be established that ensures, over and above distributions to Clubs and racing industry participants, that with these expenditures growing at a rate of around 4-5% per annum that they were able to be funded under the model into the future.

6.3.2.2 **WA Racing Industry Distributions, Subsidies and other Funding**

Given the previous various discussions throughout this Report about the history of the distributions to the WA Racing Industry over the last few years and particularly the 5 years to 2012/13, the following statements are made to attempt to suggest a potential outlook for wagering revenue growth and hence potential WA Racing Industry funding growth :

- With declining pari-mutuel betting the overall wagering growth for TAB's have been limited to around 1.2% per annum over the last four years with no reason to believe growth rates over the next 5 years will significantly differ from this. An overview of some financial market/gaming market analysts' outlooks for the Australian TAB wagering revenue growth over the next few years do however suggest some improvement in growth rates. Whilst such outlooks do vary substantially, and also differ between Tabcorp and Tatts, an outlook of around 2% growth on average is broadly expected.
- The low growth performance of other TAB operations has reflected declining retail pari-mutuel turnover offset by strong fixed odds turnover growth.
- WATAB/RWWA's ability to generate growth in its wagering turnover and revenues over this recent period, as explained earlier, arose from its delayed developments in on-line and retail information and betting systems that have essentially enabled it to catch up to other TAB's, as well as its growth in premium punters and improved margins from more favourable pooling arrangements.
- In acknowledging this growth, in the last 3-4 years, the growth in distributions has been constrained by the cash reserving practices of RWWA which has withheld some of the wagering revenue growth from the WA racing industry.
- Flowing from the above, and with more recent investment in its on-line (particularly mobile) and SST capabilities, the future wagering turnover growth and existence of cash reserves to average out oscillations in such growth would suggest an ability to fund funding growth at wagering turnover growth levels similar to those recently experienced for up to another five years potentially.

- In addition to the previous point, it would appear that WATAB/RWWA has begun to, and will for a period, experience similar fixed odds growth with retail pari-mutuel decline, albeit the latter less pronounced because of upside still inherent in WATAB/RWWA's underlying retail business.

Taking these points above, it is reasonable to suggest the WATAB/RWWA under its existing structure could realistically be expected to grow WA Racing Industry distributions at around the 3.5% per annum compounded rate of recent years potentially over the next five years to a level of in the vicinity of $150 million in financial year 2018/19. All other WA Racing Industry funding by RWWA would also be able to grow at a similar rate. This is predicated, as outlined above, on the availability of cash reserves to underpin fluctuations and impacts on this growth rate in that period, some but limited further growth in premium punters, and general benefits flowing from investments by RWWA in developments not being inhibited by any regulatory change. (An actual forecast growth outlook will need to be provided by RWWA).

Clearly this suggested outlook for WATAB/RWWA wagering turnover growth going forward would need to be rigorously tested and assessed in a potential privatisation process. The growth rate estimate is simply based on a view of the ability to continue on a similar growth path as experienced in recent years. A much more detailed forecasting process by RWWA with much more information would be required to establish a more informed outlook.

When discussing the base line and future funding position of the WA Racing Industry under a potentially privatised WATAB, the baseline needs to include **all** current funding provided by WATAB/RWWA. Throughout various parts of this Report there has been references to Distributions to the Racing Industry (Racing Clubs and Participants), subsidies/payment made to or on behalf of Racing Clubs by RWWA, funding of training facilities, other grants and subsidies, and the operating costs of RWWA conducting its Racing Operations and integrity roles and other PRA responsibilities. These total funding amounts are not readily able to be fully determined for this Report, but are understood to possibly represent approximately another $25-26 million annually on top of the Distributions and Grants paid to Racing Industry Clubs and Participants.

Again, this total Racing Industry funding would form the basis for the current and the projected minimum funding obligations (reflecting the expected WATAB/RWWA growth profile over the next 5 years) to apply in the WA Racing Industry funding model under a potential privatisation of WATAB.

As also discussed throughout this Report, RWWA has over the last few years been building up its cash reserves to provide a buffer capacity to any detrimental impacts on wagering inflows so as to manage or smooth WA Racing Industry funding through any such impacts. The following table sets out the Distributions and Grants to the Industry, the reported profit/loss of RWWA for the year, and the Cash and Cash Equivalents held at the end of each financial year (as derived from RWWA Annual Reports) :

	$ million			
	Distributions and Grants	Profit /(Loss)	Profit before Distributions	Cash and Cash Equivalents
2007/08	104.637	6.455	111.092	71.939
2008/09	110.146	(11.877)	98.269	47.990
2009/10	106.498	(1.448)	105.05	42.251
2010/11	107.551	(8.991)	98.56	39.583
2011/12	113.798	10.858	124.656	56.174
2012/13	117.665	9.302	126.967	67.745

Clearly in hindsight RWWA probably grew distributions prior to 2009 a little too quickly without reserving, so that then when the adjustment was needed it hit particularly Racing Clubs distributions directly and hard. The year 2009/10 includes the delayed recording of $11.0 million of racefield fees actually relating to 2008/09. When these figures are therefore adjusted the impacts to WATAB/RWWA in 2009/10 carried into 2010/11 are clear to see. Since that time profitability can be seen to have grown much more than Distributions and Grants to the Racing Industry, and Cash Reserves have been able to be built up, with Racefield Fees appearing to have increased significantly in 2011/12 (perhaps suggesting increased corporate bookmaker payments).

It is understood that in 2013/14 Distributions and Grants increased to $130.8 million whilst profit levels are believed to have been maintained. Such prudent risk management by RWWA should be seen positively and constructively in a medium/long term sense despite the more subdued growth in WA Racing Industry funding. However, in a privatisation process such cash reserves should not be lost to the WA Racing Industry given both the reason and the history of funding behind the existence of these cash reserves. Higher distributions and/or infrastructure funding could otherwise have been funded from the improved performance of WATAB.

6.3.3 **No Worse Off**

The earlier discussion in Chapter 5 of this Report on the current total funding of the WA Racing Industry outlined the fragile nature of the existing position based on distributions from WATAB/RWWA's wagering activities and the investment by owners based on reasonable levels of stakes prizemoney. Accordingly, any potential WATAB privatisation would require that the WA Racing Industry (including the PRA) is "no worse off" in terms of its financial and risk profile as a result of the privatisation. In general terms this means that the funding outcome of a potential privatisation to the WA Racing Industry reflects what WATAB/RWWA has been able to achieve and is forecast to achieve into the future and that the risk profile does not materially change to put such funding at greater uncertainty in terms of levels and security. This context of no worse off is to be pursued in relation to total WA Racing Industry funding, and should not be interpreted as applying to any underlying component parts of that total funding level.

In defining "no worse off" in a more direct way and with clarity, it is both of these perspectives that need greater explanation.

6.3.3.1 "No Worse Off" Funding

The perspective for "no worse off" funding must be two-fold – to establish a base at the time of privatisation that reflects the current funding level – and to establish a future perspective that at least ensures no less funding than that which WATAB/RWWA would have provided in the absence of privatisation. The earlier analysis in Chapter 5 of this Report has outlined why anything less than the current funding level as the base is simply a formula for a significantly smaller WA Racing Industry that neither a new wagering operator, nor the WA Government, should/would wish to entertain as an outcome of privatisation.

As discussed above, whilst clearly the author is not privy to the forward estimates and detailed planning of RWWA, it has been hypothesised that similar growth profiles over the next 5 years to those in the last 5/6 years would seem to be possible. The validity of the figures will need to be established in any potential privatisation, but the principle of this definition of "no worse off" funding is one the WA Racing Industry must seek to establish as a requirement of the racing industry funding arrangement to be put in place in such a potential privatisation.

The delivery of such a commitment by a new wagering operator post privatisation has aspects associated with the racing industry funding arrangement, the privatisation legal structure, and the governance framework. However, to establish certainty on such levels of funding for a certain period, the only model is to legislate/regulate within the relevant document (be it one or more of legislation, regulation, licence or legal agreement) mandated minimum payments to be paid by the new wagering operator to the WA Racing Industry. Whilst such an "underwriting" requirement will create a risk profile to a potential new wagering operator, this will be mitigated by the impact on the value that bidders will be prepared to offer in the privatisation and a good understanding of the WA wagering market and of WATAB's position in it.

All of this is obviously predicted on an acceptance of WATAB/RWWA's current and potential future performance outlook, which will be hotly debated but this principle is the important fact to establish.

The period of the "underwrite" of performance is also of prime significance here. In the latest Victorian wagering licence the period was established as three years. This will be a point of contention with any prospective bidder.

Once such an "underwrite period" completes, or immediately in the case where such an arrangement is not put in place, under most models of privatisation the funding of the racing industry will most probably rely on the financial performance of the new wagering operator from a revenue/margin, profit or combination of both perspective. This takes us into the next section on risk.

6.3.3.2 "No Worse Off" Risk

The WA Racing Industry is currently effectively exposed to the risk of the wagering performance of WATAB/RWWA. This risk is mitigated somewhat by the influence it is able to bring through its RWWA Board composition, and was in essence the basis upon which the WA Racing Industry accepted this risk, together though with acknowledging also that the remuneration level for its product property rights are partly a reflection of wagering performance, but within the context of a valuable exclusive retail wagering authority. Again, having a role in Board composition and through Consultative Committees provides a basis also for influence in this regard. This risk in recent times and into the future for a certain period has also been tempered by the build-up of cash reserves within RWWA to provide a protection mechanism to future WA Racing Industry funding from any aberrations in WATAB/RWWA's future wagering performance.

Such mitigates will not exist in most privatisation models, with only the joint venture type models providing some reflection of decision-making mitigation in relation to wagering performance (depending upon the exact model adopted).

In addition, as identified earlier, in a potential privatisation there are issues around the continuity of the extent of premium punters, and the prospect for the channelling of account customers to lower cost jurisdictions of the new wagering operator, that add additional risk in a privatisation. Of course, offsetting these factors will be the matters of potential improvements in the fixed odds offer and hence revenue, and more rapid future rollouts of technologies and products (if timely regulatory permission is provided). Specific other risk management approaches such as licence and legislative requirements for the wagering operator to operate in the best interests of the WA Racing Industry, monitoring and/or reporting, or more specific contractual provisions, can also be considered. The risk profile will change and the structures for privatisation and the WA Racing Industry funding models need to be established to ensure these risks are mitigated to the best possible extent so as to provide the WA Racing Industry with a "no worse off" risk outcome.

In this context it is therefore recommended that if such arrangements do get put in place under a privatisation process that the WA Racing Industry also seek that at the completion of the mandated minimum funding obligation time period that a review process be included in the structure to examine the racing industry funding model at that time to ensure it appropriately reflects the then current wagering performance and conditions.

What Does All Of This Mean For The Western Australian Racing Industry?

This Report has discussed in some depth the financial situation and operations of RWWA, the national and Western Australian wagering markets and WATAB/RWWA's performance and position within the market, the financial value chains of participants within the Racing Codes that make up the WA Racing Industry, the funding of the Industry, what privatisation means and how it could occur for WATAB, and with all of this what the potential implications of the privatisation may be for the WA Racing Industry. This chapter will talk through what all of this means for the WA Racing Industry, and suggests positions that could be adopted and potential actions to be taken by the WA Racing Industry in relation to the possible privatisation of WATAB.

7.1 The Question of Privatisation of the WATAB

As has been established in this Report, Western Australia is now the only Australian jurisdiction in which the TAB wagering operation is government owned, with the TABs in all other States and Territories owned and operated by either Tabcorp or Tatts Group. Given the very significant competition from corporate bookmakers and other TAB's (with the end of the Gentlemen's Agreement) in relation to racing wagering, and the general competition of sports wagering which is growing at a much faster rate than race wagering, from an Australian wagering industry outlook viewpoint it is difficult to support long term government ownership of an Australian wagering operation. Whilst some will point to successfully operated government-owned wagering operations overseas (such as the Pari-Mutuel Urban in France), these are national entities, not state based, and hence of size and position to better face the competition of on-line bookmakers.

It is in this competitive context that Tabcorp and Tatts have looked to acquire other TAB operations to get such scale. This scale enables them to meet the costs of funding the local racing industries and continuing to invest in technologies, product offers and retail-based infrastructure to sustain their businesses under strong competition. WATAB/RWWA's wagering turnover is not large enough by itself to ensure the liquidity and price stability in its wagering pools for a competitive pari-mutuel wagering offer, and hence has a long running pooling agreement with Tabcorp (into the SuperTAB pool) to provide these attributes. WATAB/RWWA's fixed odds turnover has not been sufficient to justify building its own in-house fixed odds management capability, and it has appropriately sought to outsource such management to existing operators with the necessary infrastructure.

In Chapters 4 and 6 this Report discussed the low growth outlook for TAB turnover and revenue around Australia. With relatively high fixed cost structures of TAB operations given the retail network and infrastructure and the associated technology costs, scale is the only answer to the required continued investment to sustain the business.

WATAB/RWWA has performed well relative to other TAB's in turnover growth terms in recent years, which does reflect a combination of solid management with a significant element of catch up to other TAB's in terms of product, retail and technology offers at levels that TAB's in other jurisdictions had previously rolled out to their customer base. Some more recent initiatives by WATAB/RWWA such as racewall technology, the improved fixed odds offer generally, and increasing levels of self-serve terminals, should continue to provide solid growth over the medium term at growth rates that should be above the expected overall national TAB turnover growth levels. However, once these catch up elements are exhausted there is no reason to suggest that WATAB/RWWA has any capacity to further outperform. In fact, to the contrary, once these catch ups have occurred, it is difficult to see how WATAB/RWWA continues to compete given its lack of scale, and the risk of its dependencies on external providers for pooling services and management.

Accordingly, the position of "if it ain't broke don't fix it", whilst understandable, needs to be seen in the context of the future wagering outlooks, the pooling dependencies, the continued competition faced, and the difficulty and necessity for continued investment that this situation requires. This is particularly problematic in an entity still faced with the implications of government ownership.

Concerns expressed about whether participants, and particularly owners, would continue to invest in the WA Racing Industry if WATAB was not government owned are answered by this situation applying in all other parts of Australia. However, in saying that, the key plank underpinning this is that under a privatised model the racing industry funding model for the WA Racing Industry must be such as to instil this confidence to continue to invest through the establishment of a racing industry funding model that ensures the funding from the WATAB wagering operator to the WA racing industry is sufficient on an ongoing basis to sustain the industry.

Having said this there are a number of other issues or concerns in relation to the potential privatisation of WATAB that weigh against proceeding with the privatisation. These issues include:

- The implications of a privatisation for the substantial premium punter component of WATAB wagering turnover, which is understood to possibly represent up to 20% of turnover. If this was to be lost because of privatisation the funding capability for the WA Racing Industry would be substantially depleted.
- The same outcomes could occur if a new wagering operator sought to move WATAB's account customers to another licence that is lower cost and hence makes these WA customers then more valuable to the operator. It is understood that these account customers could represent up towards 25% of WATAB's turnover, and hence represent a significant potential risk
- In some Australian jurisdictions the privatisation processes themselves have not been seen to work well, with arguably suboptimal outcomes for the Government and the Racing Industry. It must however be recognised that in some cases this has most probably been because of existing inherent issues with the management of the underlying Racing Industry or the TAB, rather than necessarily attributing all or any blame to the actual privatisation process itself.

- Whether the WA Government is prepared to engage and spend the time with the WA Racing Industry to convince the Industry that it will be no worse off.
- Would the WA Government be better placed prioritising assets for sale that weigh on the public purse and hence that are not in the position of WATAB/RWWA and the WA Racing Industry of essentially self-funding itself (except perhaps infrastructure) and contributes in excess of $40 million per annum to the WA Government in wagering taxes.
- Is it currently worth privatising WATAB given the value equation for a new private operator that needs to service the requirements of new stakeholders such as the Australian Taxation Office (income tax) and shareholders (dividends) in addition to maintaining the obligations to the WA Racing Industry, the WA Government, and other existing stakeholders.
- Clearly a new privately owned wagering operator of WATAB will have a primary focus on returns to its shareholders that may not result in decision-making by that operator in the best interests of the WA Racing Industry.

There are a number of these matters that can be dealt with by the WA Government in a potential privatisation process, if they so choose, to ensure the position of the WA Racing Industry is protected if a privatisation of WATAB is to occur. If these matters are not appropriately addressed, then WA Racing Industry would seriously need to consider opposing a privatisation of WATAB.

Accordingly, and subject to a number of issues raised above being addressed prior to any privatisation, the WA Racing Industry should acknowledge that the privatisation of WATAB is, on balance, likely to occur at some time over the next few years. Even given this situation the WA Racing Industry should only countenance such a privatisation of WATAB if the racing industry funding model leaves the industry in a at the least “no worse off” financial position, and the governance and licence frameworks ensure the WA Racing Industry is protected in terms of its risk profile and has a no less favourable standing in the context both of potential privatisation and future wagering licencing process outcomes.

Whilst there is the prospect of arguing over the actual ownership of the WATAB, and also to raise the question of racing program product rights ownership, it is recommended that the WA Racing Industry not seek these actions if the WA Government, in any potential privatisation process, agrees to an acceptance of at the least a no worse off funding model that is encapsulated in legislation and contract and links the resulting obligation to fund the WA Racing Industry to the granting of the licence, with retail exclusivity the key driver of value and racing industry funding obligations.

7.2 The Current Situation of the WA Racing Industry

In Chapter 5 of this Report a picture of the operation and financial position of the WA Racing Industry and its participants was provided in a great deal of detail. The overall perspectives to take from this value chain analysis of the WA Racing Industry are:

- The distributions, subsidies and other payments make to the participants in the WA Racing Industry by RWWA from its WATAB wagering operations have just been sufficient to support the Industry, but on many indicators there has been some significant Industry contraction in recent times.
- Given that the WA Racing Industry has calibrated to the current funding levels, despite increased costs growing faster than returns in most cases, there is no room in the value chains for any less funding from wagering.
- With the punters and owners being the major funders of the WA Racing Industry, and for owners the investment being largely aspirational and seeking intangible returns, any reduction in the wagering contribution to the WA Racing Industry which reduces stakes prizemoney would quickly also reduce owners' investment (based on an acceptable loss context), leading to a higher leverage downwards to racing industry funding than just the distribution reduction.
- The code value chains illustrate that whilst a small number of participants in the Western Australian Racing Industry generate a reasonable return from racing, most are not. It is an Industry in which a small number of people in each segment tend to take a disproportionate share of returns leaving a number to battle financially within the model. In many cases, particularly with owners and some breeders, it is not racing that has created wealth, it is external wealth, and in fact racing tends to reduce this wealth. Racing may often be called a sport of kings, but in most cases it attracts "external" kings, it does not create them in a wealth sense from Western Australian racing.
- Accordingly, there are many in the WA Racing Industry who know nothing else and generate little return but the passion of the Industry. Many employees would have some difficulty finding alternative employment, and operate around minimum wage rates (if that).
- In many cases Racing Clubs survive through voluntary and honorary roles at Board/Committee and operation levels, with Clubs as a whole only breaking even financially on the back of various subsidies paid by RWWA from its wagering returns. The combined Racing Club financial figures reflect that there is no capacity to reduce funding to the WA Racing Industry without significantly damaging the financial position and hence potential sustainability of many of Western Australia's Racing Clubs.
- Given the tight operational financial position of the WA Racing Industry, and the need for property holdings availability to breed and train animals for racing, property assets for those who can obtain them become not only operational assets but represent the only form of retirement/superannuation they hold, the value of which is often tied to the sustainability of the industry.
- With its current settings, the WA Racing Industry is effectively just self-funding on an operational cashflow basis, but infrastructure funding to maintain and improve, and keep safe, existing facilities is an ongoing challenge.

Accordingly, the Western Australian Racing Industry currently is somewhat calibrated in a fragile fashion to the current funding structures in terms of distribution, subsidies and other payments from WATAB/RWWA, whilst the WA Government nets over $40 million per annum from the Wagering Tax.

Any action that reduced funding to this current balanced but fragile situation would therefore clearly very quickly and directly disrupt this position and lead to significant pull backs across the WA Racing Industry as there are no real buffers to absorb any significant reductions in funding. So any racing industry funding model that did not sustain the current funding levels, nor provide some certainty on future funding, would not only immediately impact the WA Racing Industry but would also quickly reduce investment given the hit to confidence it would represent. Some signs of this are already evident from the current uncertainty in the WA Racing Industry from asset infrastructure and TAB privatisation discussions.

7.3 **WATAB/RWWA**

The wagering performance of WATAB/RWWA has been identified in this Report as solid in recent times in managing the process of catching up with other TAB operators, and in some sense partially protected by a degree of punter loyalty to the local product (as opposed to corporate bookmakers) and from Racing Clubs agreeing not to seek sponsorship of corporate bookmakers to promote their product. This performance would however have seemed to come from a greater focus by RWWA on its wagering responsibilities than its racing responsibilities. Whilst there is some evidence that RWWA has now sought to achieve a better balance in its focuses in this regard, it has probably not in recent times invested enough resources and focus in the quality, integrity and promotion of the racing product.

This situation would appear to have led to an environment where industry participants in general have been reasonably pleased with the distributions, subsidies, and other payments, and bonus/incentive schemes put in place, by RWWA to fund the Racing Clubs and racing industry participants, but have expressed some frustration with elements of the management of the racing product. Whilst it is clearly a difficult, if not impossible, task to satisfy all stakeholders across all Codes in the racing industry, discounting this out still seemed to leave a generality around concerns on RWWA's performance in this regard.

The focus to wagering has until recently been predominately in relation to off-course wagering in the context of retail and digital predominately, with limited attention to on-course wagering. The resulting drop in on-course wagering (which also can be attributed to declining attendances and competition from corporate bookmakers), when combined with no recent growth in Racing Club distributions by RWWA (until very recently) with increasing cost pressures faced by Racing Clubs, has resulted in Racing Club concerns regarding RWWA's performance. The subsidies around racefield fee payments on Club's behalf, as well as broadcasting expenses and similar payments, funded by RWWA need to be considered here though, as too does the need for Clubs to get patrons back to the races.

The generally favourable perspective on RWWA's financial performance is however an area of major risk and possible concern for the WA Racing Industry under a potential privatisation of WATAB. It needs to be clearly explained and made clear to the WA Government that this is not simply a statement about stakes prizemoney funding. As can be very clearly seen from Chapter 5, the returns generated by the wagering operations of WATAB/RWWA and provided in funding to the WA Racing Industry included:

- Stakes prizemoney funding
- Event fee payments to Racing Clubs
- Training funding to Racing Clubs and RWWA training facilities
- Jockeys and Drivers payments
- Breeders and Owners Bonus / Incentive Schemes
- Product fees, broadcast costs and other payments on behalf of Racing Clubs
- Cost of RWWA's Racing Operations groups

In the event of a privatisation of WATAB it is all of these (and any other payments made by RWWA to the WA Racing Industry not identified above) that would need to be catered for in the funding arrangements to be put in place between the wagering operator and the WA Racing Industry.

In addition, RWWA has been building cash reserves which it is understood has occurred to provide an ability to smooth distribution levels to protect against events such as those that resulted in a distribution decrease in 2009/10. There are three matters of interest in relation to these cash reserves for the WA Racing Industry in any potential privatisation of WATAB:

- These cash reserves should be retained by the WA Racing Industry
- Such reserving / smoothing will not be an element of a privatised wagering operators approach
- The potential for an entity such as Racing Western Australia to have such a reserving capability into the future

These matters need to be pursued with the WA Government in any discussions on the potential privatisation of the WATAB.

7.4 WA Racing Industry Positioning in a Privatisation

Throughout this Report, and particularly in Chapter 6, it has been shown that privatising / selling a TAB business is a complex matter, with many moving parts, many stakeholders, and many issues requiring close consideration and decision, to determine whether in fact privatisation should proceed, if so in what form and structure, and for what value. Many of these interrelated considerations will not just go to matters of value to be realised in a sale process but also to risk positions of the parties prior to and then subsequent to the privatisation.

In this context it is critical for the WA Racing Industry to determine with the WA Government what the Government's objectives of the privatisation of WATAB are so as to ensure the Industry's interests are protected. Without pre-empting what the WA Government's position may be, if it does seek to privatise the WATAB, is its objectives one or more of the following in any potential privatisation:

(i) To remove Government from the ownership of its wagering business because it does not believe government ownership in the competitive industry is appropriate

(ii) To ensure that the WA Racing Industry's interests are fully protected and that the Industry is no worse off from the transaction

(iii) To maximise the sales proceeds with or without point (ii) as a consideration

(iv) To privatise the WATAB because the Government believes it has reached its maximum value in terms of its potential sale value due to future revenue growth outlooks and competitive pressures

(v) To establish licence terms and conditions and legislative frameworks that enable review points for the arrangements or lock them in long term, and provide more or less flexibility and WA Government involvement in the conduct (but not the operation) of the wagering licence than currently exists.

The WA Racing Industry will clearly look to have point (ii) above as a primary objective in any potential WATAB privatisation process if it is to occur, and so long as this is ensured and no worse off is clearly and unambiguously defined and agreed in funding and risk profile terms, the Industry should be prepared to accept the WA Government seeking its value.

In this context of value, whilst clearly a WA Government issue, it is imperative that if a sale is to occur that the medium term wagering performance outlook of WATAB/RWWA as suggested in this Report is reflected in the value. This can occur in two ways that the Racing Industry would seek to have in the process:

- Acceptance of the above market wagering performance expectation for the medium term
- No worse off definitions to incorporate this outlook into a mandated minimum guaranteed underwritten funding commitment to the WA Racing Industry for an initial period.

Whilst potential bidders will reduce their valuations for the latter point, acceptance of the former through strong justification by RWWA Management (if this is in fact the case) to potential bidders should mitigate a good degree of this risk in the valuation process.

7.4.1 No Worse Off

Section 6.3.3 of this Report discusses the perspective of “No Worse Off” for the WA Racing Industry if a privatisation of WATAB was to occur. It identifies the two perspectives to “no worse off” as encompassing both funding and risk profile.

The fragile calibrated financial model of the WA Racing Industry necessitates a “no worse off” funding position as being the current level of distributions, subsidies, incentive/bonus schemes, costs of racing operations and integrity, and other payments made by RWWA to Racing Clubs and WA Racing Industry participants. Going forward, it defines “no worse off” funding to be reflected in mandated minimum payments levels over the next five years that reflect the estimated expected WA wagering industry performance in wagering turnover growth from WATAB in a no privatisation scenario. It would be anticipated that this performance could at the least be based on an expectation of continuing recent growth rates which have been around 3.5% per annum. Of course, this would provide a minimum mandated level of future payments, with better wagering growth performance by a privatised WATAB producing higher payments to the WA Racing Industry. This will need to be formally assessed through detailed forecasting by RWWA. After that time the WA Racing Industry would be exposed to the wagering industry performance more generally (as would occur under no privatisation), but should look to a process to review the ongoing WA Racing Industry funding model at that point so that it is based off the conditions and performance at that time.

In terms of risk profile, Section 6.3.3.2 talks to the point that the WA Racing Industry's funding risk is primarily and largely subject to WATAB's wagering performance now, but is mitigated to an extent by the RWWA Board composition requirements around Code representation, and through the Consultative Committees for each Code with RWWA (although these are more directed at racing issues than funding). Also the cash reserving now occurring within RWWA won't be a practice specifically for the WA Racing Industry by the new operator of WATAB under a privatised model.

As outlined above, the ability for these cash reserves to be maintained by the WA Racing Industry needs to be clarified (including whether the legal structure of an entity such as Racing Western Australia could undertake this).

In governance terms, a joint venture structure would position the WA Racing Industry in a situation close to but not the same as currently with WATAB/RWWA in terms of some oversight and decision-making influence of wagering operations. The funding models also suggested in this Section would add to such risk mitigation. This will need further consideration once more detail is known on the possible structures and funding models for a potential privatisation.

7.4.2 **Other Privatisation Issues**

This Report, particularly in Section 6.2, has outlined a number of the issues that need to be worked through in a potential privatisation of WATAB, and in most cases indicated that the WA Racing Industry cannot and should not establish a firm position on many of these prior to having the opportunity to discuss them with the WA Government before any possible privatisation process is formally initiated.

Some commentary however on specific areas that are relevant for the WA Racing Industry to consider if WATAB was to be privatised are:

(i) The Wagering Licence – that it is an exclusive retail totalisator licence for pari-mutuel and fixed odds betting, with an obligation to meet WA Racing Industry funding. If it is to be a long term licence the WA Racing Industry should look for the licence to include shorter term review points to test the appropriateness of the racing industry funding model and operation of the licence – either through shorter exclusivity terms or similar trigger points. The WA Racing Industry would prefer to see a flexible and timely approval process for products and channels within the licence to obtain a wide product range that drives revenue for the wagering operator.

(ii) The Legislative Framework – the major focuses here for the WA Racing Industry are:

- That the legislation and licence requires the wagering operator to enter into a contractual funding model with the WA Racing Industry.
- That the legislation incorporates a no worse off (or no less favourable) requirement on any licences into the future (including this one) for the WA Racing Industry if privatisation occurs.
- That the legislative framework is not too restrictive on the operations of the new wagering operator to ensure that returns are not inhibited

(iii) Structure – it is too early at this stage to suggest a preferred WA Racing Industry position other than to state that a model under which the Government and not the wagering operator funds the industry must be avoided. Racing Industry ownership of the WATAB is not recommended.

(iv) Racing Industry Funding Model – other than the requirement for the WA Racing Industry to be "no worse off" in relation to funding, the matter of the appropriate model cannot be determined at this stage. Total reliance of a profit share model is however not recommended. Many other aspects of the potential privatisation need to be understood before a view on the desired racing industry funding model can be formed.

(v) Racing Program Agreement – other aspects such as structure and the Racing Industry Funding Model will heavily influence both how the Racing Program Agreement process is to work and the quality of the Program, but it requires an integrated Tri-Code grouping for the WA Racing Industry (which Racing Western Australia – RWWA without wagering – could bring given its existing in-house capabilities).

(vi) Wagering Tax – this is a WA Government issue other than it reduces the amount of funding available to the WA Racing Industry, but it is important for the new wagering operator and the WA Racing Industry to get certainty around this matter longer term to lock away the appropriate racing industry funding model into the future.

(vii) Racefield Fees – a "no worse off" position in relation to racefield fees at present is unclear but would probably involve the wagering operator offsetting payments against the WA Racing Industry funding and Racefield Fee income flowing to the WA Racing Industry. It is recommended that this offset mechanism for the new wagering operator under a potential privatisation be limited to no more than the amount of incoming Racefield Fees received by the WA Racing Industry each year.

(viii) Other Financial Arrangements – matters such as GST reimbursements, Fractions and Premium Player Rebates will sit with the WA Government and a new wagering operator to agree if a privatisation was to occur, but outcomes would need to be considered in finalising the WA Racing Industry Funding model. It would be recommended that unclaimed dividends on racing be paid to the WA Racing Industry after the 7 months as set in legislation at present.

(ix) On-course Wagering Arrangements – this is an area that has lacked focus by RWWA up until recently, and an area of some potential upside to all under any future models. Accordingly, this is an area, particularly for Racing Clubs, but also the entire industry, that would need to be dealt with appropriately in a potential privatisation, including consideration of the suggested improvements listed in Section 6.2.1.1.1 of this Report.

7.5 WA Racing Industry Governance Structure in a Privatised Model

If the wagering operations of WATAB/RWWA are privatised, the question of what happens with the governance of the WA Racing Industry is raised. A refocused RWWA, which after privatisation could now be Racing Western Australia and without wagering, could effectively continue to largely operate from a PRA perspective as it currently does. The difference would be rather than operating the WATAB and allocating the proceeds from wagering as appropriate, it receives the funds under the Racing Industry Funding Model from the privatised WATAB which it continues to allocate as it currently does and otherwise undertakes all of its non-wagering activities.

Given the history of the WA Racing Industry and its Codes, it is considered that the establishment of RWWA as a Tri-Code representative body of the Industry has worked reasonably well. Whilst Codes will have different perspectives on various matters as they seek to represent their particular constituents, the benefit of decision-making for the WA Racing Industry informed by knowledge across the three Codes seems to outweigh the perceived disadvantages. It would be expected that this would in fact improve with the greater racing industry focus the new entity would now have as its only responsibility.

This is a suggested way forward. There appears no real benefit in changing the current structures in place underneath this, although it is unclear why the Western Australian Greyhound Association necessarily needs to remain an entity established by statute and subject to the direction of the Minister. A structure similar to that of RWWA at present would seem appropriate for WAGRA – and accordingly it is also considered that the current structure of RWWA be retained (amended to exclude wagering responsibilities).

In this context and considering the challenges that the WA Racing Industry will continue to face into the future in the form of :

— competing entertainment and leisure time offers for potential punters and racegoers,

— significant investment in facilities by these competing offers,

— the difficulty for the WA Racing Industry (other than greyhounds to an extent) to find an offer that continually entertains within a relatively short time period (eg AFL, Big Bash cricket), and

— the WA Racing Industry dependence upon a low growth wagering based funding model of TAB's and relatively low racefield fees

such an integrated Tri-Code approach seems necessary. In fact, it seems critical that the WA Racing Industry actually look at itself as a single sport rather than 3 Codes and determine how its portfolio of entertainment and wagering offers (and **all** available assets) can best be managed to attempt to better face these significant challenges with what is a fragile economic model for racing. If such an approach is adopted it would be appropriate to re-consider the skills required on the Board to ensure the necessary re-focusing is reflected in the Board composition.

7.6 WA Racing Industry Asset Infrastructure Efficiency / Rationalisation

This last issue is no better illustrated than in the case of the infrastructure assets currently utilised by the WA Racing Industry – not just the race tracks but also the properties owned/used by participants within the Industry.

The current very tight operational cash flow position of the WA Racing Industry clearly shows extremely limited capacity to fund infrastructure maintenance and repair, let alone development and improvement to attract people to the races. The WA Racing Industry should seek in some manner a funding mechanism for ongoing infrastructure needs in any potential privatisation of WATAB. A number of possible approaches to this requirement are discussed in Section 6.2.1.14 of this Report.

However, in seeking such a requirement, the WA Racing Industry must also take the initiative and as a total industry, rather than by Code or region, seriously look at how to better use the assets available to it. Efficiency and effectiveness of current use and possible rationalisation and/or relocation must be actively considered. It would seem imperative that such a commitment by the WA Racing Industry occurs so as to be able to constructively argue for some form of infrastructure funding support in a potential privatisation process. This would seem to be the case irrespective of whether a privatisation occurs or not given the conclusion next year of the current RIGF and R4R capital funding programs for racing industry infrastructure.

Initiatives such as the recently announced Metropolitan Racing Asset Taskforce are positive steps in this regard, as is the work Deloitte are undertaking for Perth Racing. However, to achieve the maximum benefit of all of this work, it needs to be integrated/co-ordinated. The WA Racing Industry as a whole needs to be supportive of such initiatives, but such initiatives must also ensure **all** relevant stakeholders are engaged.

Whilst this issue is outside the scope of this Report, it is a critical piece of the future sustainability of the WA Racing Industry.

7.7 Other Income Streams

Whilst it would appear currently outside WA Government policy and therefore difficult to contemplate being able to successfully argue, the WA Racing Industry could look to continue to push for a couple of other product/income streams within a potential privatisation process:

- Trackside – a simulated racing events product operated by Tabcorp but for which Crown Resorts (the operator of the Crown Casino at Burswood) has the Western Australian rights. This product could be approved as a wagering product and hence only be available within TAB's and on-course.
- Racinos – certain racecourses could be provided with the ability to have gaming machines extended from the Crown Casino licence, as a way of improving infrastructure use and funding, recognising that racecourses are already places of gambling and suitably regulation compliant.

Such product expansion could provide funding to the Government, the Racing Industry, the wagering operator, and potentially in the case of Racinos the community as well.

7.8 WA Racing Industry Engagement with the WA Government over Privatisation of WATAB

The objective for the WA Racing Industry if the privatisation of the WATAB does proceed is to be able to engage with the WA Government early in its process deliberations to work with and agree with the Government the acceptable positions on the many issues of a privatisation that have been outlined in this Report. It is recommended that the WA Racing Industry seek such engagement and interaction with the WA Government prior to any formal discussions or processes commencing with potential bidders and/or a formal sale commences.

To ensure that the WA Racing Industry's, and the WA Government's, best interests are met in the privatisation process, it is critical that the WA Government is very clear on the objectives to be achieved in the privatisation/sale for the WA Government and the WA Racing Industry, and on funding models, structures, key licencing parameters and legislative and contractual frameworks to present to potential bidders. Where relevant, these will have been agreed with the WA Racing Industry and formally documented as the basis for seeking proposal bids from potential bidders in such a potential privatisation.

The vital need for this engagement, and for formally agreed positions on the many privatisation matters raised, between the WA Government and the WA Racing Industry, lies in the potential risks of not getting the privatisation of WATAB right.

These can be reflected in some previous TAB privatisation experiences where the impacts of losing account customers has impacted racing industry funding, where inappropriate consideration to premium punter responses led to significantly overstated value expectations, and to the situations where funding arrangements and wagering tax settings have needed to be amended to ensure better racing industry funding. Early engagement and agreement on frameworks, objectives and expectations between the WA Government and the WA Racing Industry will significantly mitigate the risks of unexpected and poorly structured outcomes for all parties, including the new wagering operator of WATAB if a privatisation does proceed.

In this context, the Western Australian Racing Representative Group will need to obtain a mandate from the WA Racing Industry to undertake such discussions with the WA Government, and seek a commitment from the WA Government for such engagement at the front end of a potential privatisation process. Such engagement must come with a requirement for obtaining agreement between the WA Government and the WA Racing Industry on the relevant industry issues identified in this Report for a potential WATAB privatisation.

This early engagement and agreement on positions for a WATAB privatisation between the WA Government and the WA Racing Industry is considered to be the best risk mitigation strategy for the "sellers" when dealing with experienced wagering operators, and some who have also been involved in previous privatisation processes.

It is particularly important for the WA Racing Industry to have a clear and documented commitment with the WA Government on the privatisation framework. Such a process occurred within the 2012 wagering licence bid process in Victoria, based on the no less favourable (ie, no worse off) requirements within the legislative licencing provisions surrounding the new licence.

APPENDIX 1

RETURN TO OWNERS – CODE COST TO RACE RATIOS

Thoroughbreds – RTO

Average Annual Cost to Owners =	$29,284(A)
Average Annual Returns =	$11,246(B)
Returns to Owners (RTO) =	**38%**

(A) Asumptions

- Excludes purchase price of thoroughbred, GST and insurance cost components
- Westspeed eligible
- Thoroughbred commences racing at age 2yo
- Average racing life 2.5 years (4.5yo at retirement)
- Horse is in work for 8 months of season
- Horse races fortnightly (10-16 starts per season)
- Average daily training rate of $70 (8 months = $16 800 annual)
- Average monthly pool/track costs of $100 (8 months = $800 annual)
- Average daily agistment rate (non-racing) of $22 (4 months = $2 640)
- Average annual dentist/chiropractor/farrier/worming/supplements costs of $2 180
- Average annual transport costs of $2 400 (allowing provincial – Bunbury, Northam, Pinjarra return metro twice a month for 8 months)
- No major injuries and thus no major veterinary costs
- Horse completes 7 trials prior to retirement (with jockey, not apprentice riding)

Thoroughbreds – Total Average Cost to Owner Table

Pre-Race	**Cost (Annual)**	**Cost (Total lifetime)**
Agistment, Breaking, Handling, Magic Millions & Westspeed Bonus Schemes	**$ 5,384***	**$13,460**
Racing		
Training	$16,800	
Agistment (non-racing)	$ 2,640	
Trials	$ 140	
Transport	$ 2,400	
Chiro/Worm/Farrier/Dentist/Supplements/ Vet (Minor treatments)	$ 1,120	
Track/Pool usage	$ 800	
Sub-Total	**$23,900**	**$13,460**
TOTAL	**$29,284**	
GRAND TOTAL RACING COST		**$86,670****

*Total pre-race cost divided by racing years (2.5)

**GrandTotal racing cost (annual racing cost multiplied by 2.5 earning years) plus Pre-race/One-off Total ($23,900 X 2.5) + $13,460

APPENDIX 1

(B) Inclusions for Annual Returns

- Base stakes (specific owner percentage)
- Feature stakes (specific owner percentage)
- Westspeed Bonuses (specific owner percentage)
- Club Training funds (designed to offset Club and owner usage costs and maintain upkeep of facilities to training)

Thoroughbred Distribution	Return opportunity 2012/13
Base Stakes	$35,108,957
Feature Stakes	$ 5,802,291
Westspeed	$ 3,218,800
Training	$ 2,316,800
TOTAL	**$46,446,848**
Individual Starters 2012/13	**4,130**
Available returns divided by starters	**$11,246**

APPENDIX 1

Harness – RTO

Average Annual Cost to Owners = $23,782(A)

Average Annual Returns = $ 9,060(B)

Returns to Owners (RTO) = 38%

(A) Asumptions

- Excludes purchase price of standardbred,, GST and insurance cost components
- No cost to owners for Westspeed nomination
- Standardbred commences racing at age 2yo
- Average racing life 6 years (8yo at retirement)
- Horse is in active work (non-stand down nor non spelling) for 9.5 months of season
- Horse is in stand down or spelling for 1.5 months of season (non-consectuively)
- Horse races weekly (15-30 starts per season)
- Average daily training rate of $47.40 (9.5 months = $13 300 annual) – this rate is deduced from averaging higher and lower rates ($60s and $35s)
- Average daily agistment rate (non-racing/stand-down) of $22 (1.5 months = $1 870)
- Average annual dentist/chiropractor/farrier/worming/supplements costs of $1933
- Average annual transport costs of $4 275 (allowing from Byford to Bunbury, Northham, Pinjarra, GP return three times a month)
- No major injuries and thus no major veterinary costs
- Horse completes average of 4 trials as unraced an average of 1 per year whilst racing (Total trials = 10)

Harness – Total Average Cost to Owner Table

Pre-Race	**Cost (Annual)**	**Cost (Total lifetime)**
Agistment, Breaking, Handling	**$ 1,600 ***	**$ 9,600**
Racing		
Training	$14,000	
Agistment (non-racing)	$ 924	
Trials	$ 250	
Transport	$ 4,275	
Chiro/Worm/Farrier/Dentist/Supplements	$ 1,933	
Vet (Minor treatments)	$ 800	
Sub-Total	**$22,182**	**$ 9,600**
TOTAL	**$23,782**	
GRAND TOTAL RACING COST		**$142,692****

*Total pre-race cost divided by racing years (6)

**GrandTotal racing cost (annual racing cost multiplied by 6 earning years) plus Pre-race/One-off Total ($22,182 X6) + $9,850

APPENDIX 1

(B) Inclusions for Annual Returns

- Base stakes (specific owner percentage)
- Feature stakes (specific owner percentage)
- Westbred Bonuses (specific owner percentage)
- Club Training funds (designed to offset Club and owner usage costs and maintain upkeep of facilities to training)

Harness Distribution	Return opportunity 2012/13
Base Stakes	$16,737,367
Feature Stakes	$ 2,795,496
Westbred	$ 1,107,600
Training	$ 447,787
TOTAL	**$21,118,250**
Individual Starters 2012/13	**2,331**
Available returns divided by starters	**$9,060**

APPENDIX 1

Greyhounds – RTO

Average Annual Cost to Owners = $5,102* or $6969** or $5,984(A)

Average Annual Returns = $5,956 or $5,711 # (B)

Returns to Owners (RTO) = 117%* or 85% or 95%# (99% average)**

**Self-bred local pup*

***Imported pup*

#Imported ready-to-run greyhound

(A) Asumptions

- 50:50 model is adopted by majority of professional trainers (and is common nationally)
- 50:50 model represents 100% ownership costs and returns shared between trainer and owner
- Average cost for 'bred' pup = $833 (Total litter cost as owner of bitch = $5,000; average of 6 pups in litter; includes stud fees, DNA, insemination, travel to vet clinic, blood tests)
- Average cost of imported pup or ready to race greyhound = $5,000
- Average rearing costs (4 months – 10 months) @ $200 per month ($1,200 total)
- Average pre-education/pre-training costs @ $70 per week for 11 weeks ($770 total)
- Interstate travel – rearing costs ($1,200)
- Average breaking cost = $400 (4 weeks @ $100 per week)
- Average immunisation and microchip costs ($115 total)
- Greyhound commences racing at age 18 months
- Average racing life 2.5 years (4yo at retirement)
- Greyhound is 'racing' weekly for approximately 5 week at a time
- Average total racing starts in lifetime = 50
- Average monthly vet/worming and flea costs of $100 ($1,200 annually)
- Average monthly food costs $180 ($2,160 annually)
- Average annual transport costs of $1,360
- No major injuries and thus no major veterinary costs
- Greyhound completes average of 12 trials prior to retirement

APPENDIX 1

Greyhounds – Total Average Cost to Owner Table

Pre-Race	Cost (Annual)	Cost (Total lifetime) or one - off
Imported pup purchase OR		$5,000 OR
Self-bred pup (local bitch) OR		$ 833 OR
Imported Ready to Race greyhound		$5,000
	$3609 or $1742 or $2584*	
Rearing		$1,200
Breaking		$ 400
Pre-Education/Pre-Training		$ 770
Immunisation/Microchip		$ 115
Transport		$1,360
Registration & Naming		$ 77
Racing		
Food	$2,160	
Worm/Flea/Minor Vet	$1,200	
Trials		$100
Sub-Total	**$3,360**	**$4,022**
TOTAL	**$5101 or $6969 or $5944#**	**$9022 or $4355 or $6460#**
GRAND TOTAL RACING COST		**$17,422 or $12,755 or $14,860 (Average of $15,012)****

*Total pre-race cost divided by racing years (2.5yrs)

**GrandTotal racing cost (annual racing cost multiplied by 2.5 earning years) plus Pre-race/One-off Total ($3360 x 2.5) + $9022 or $4355 or $6460

#Imported ready to race greyhound assumes only transport and trial costs as “one-off/pre-race costs”

(B) Inclusions for Annual Returns

- Base stakes
- Feature stakes
- Westcha$e Bonuses (excluded from returns for imported ready-to race-greyhound)
- Club Training funds (designed to offset Club and owner usage costs and maintain upkeep of facilities to training)

Greyhound Distribution	Return opportunity 2012/13
Base Stakes	$8,594,450
Feature Stakes	$1,274,560
Westcha$e	$ 570,750#
Training	$ 447,331
TOTAL	**$10,887,061**
Individual Starters 2012/13	**1828**
Available returns divided by starters	**$5,956 or $5,711#**

#Imported Ready to Race are not eligible for Westcha$e bonuses

APPENDIX 2

HORSE AND GREYHOUND TRAINING AWARD 2010

ATA

MINIMUM WAGE RATES

EFFECTIVE FROM 1ST JULY 2014

AGE	38 HOURS	SINGLE TIME	TIME & HALF	DOUBLE TIME	CASUAL	SUNDAY CASUAL
STABLEHAND - COMMENCEMENT *(as per award definition)*						
ADULT	640.90	16.87	25.31	33.74	21.09	42.18
Aged 20	608.90	16.02	24.03	32.04	20.03	40.06
Aged 19	512.70	13.49	20.24	26.98	16.86	33.72
Aged 18	448.60	11.81	17.72	23.62	14.76	29.52
Aged 17	416.60	10.96	16.44	21.92	13.70	27.40
Aged 16	384.50	10.12	15.18	20.24	12.65	25.30
Aged 15	352.50	9.28	13.92	18.56	11.60	23.20
STABLEHAND - GRADE 1 *(as per award definition)*						
ADULT	659.40	17.35	26.03	34.70	21.69	43.38
Aged 20	626.40	16.48	24.72	32.96	20.60	41.20
Aged 19	527.50	13.88	20.82	27.76	17.35	34.70
Aged 18	461.60	12.15	18.23	24.30	15.19	30.38
Aged 17	428.60	11.28	16.92	22.56	14.10	28.20
Aged 16	395.60	10.41	15.62	20.82	13.01	26.02
Aged 15	362.70	9.54	14.31	19.08	11.93	23.86
STABLEHAND - GRADE 2 & TRACKRIDERS *(as per award definition)*						
ADULT	684.70	18.02	27.03	36.04	22.53	45.06
Aged 20	650.50	17.12	25.68	34.24	21.40	42.80
Aged 19	547.80	14.42	21.63	28.84	18.03	36.06
Aged 18	479.30	12.61	18.92	25.22	15.76	31.52
Aged 17	445.10	11.71	17.57	23.42	14.64	29.28
Aged 16	410.80	10.81	16.22	21.62	13.51	27.02
Aged 15	376.60	9.91	14.87	19.82	12.39	24.78
STABLE FOREMAN *(as per award definition)*						
	746.20	19.64	29.46	39.28	24.55	49.10
TRAINING ASSISTANT *(as per award definition)*						
	769.60	20.25	30.38	40.50	25.31	50.62
TRAINER *(as per award definition)*						
	814.20	21.43	32.15	42.86	26.79	53.58

14. ALLOWANCES (Sub-Clauses extracted from the Horse & Greyhound Training Award 2010)

14.1 Racecourse attendance allowance
Every employee who is required to attend a race meeting must be paid a racecourse attendance allowance calculated as follows:

(a) $ 23.70 attendance at a race meeting within 75 kilometres of the employee's place of employment,
or $ 23.70 plus $ 5.58 for each 50 kilometres (or part thereof) at a race meeting held more than 75 kilometres from the employee's place of employment

(b) $ 10.77 meal allowance for each meal unless the employer supplies the meal.

14.6 Boots, cap and vest allowance
Track riders (including people required to drive or ride horses) must be paid an allowance per week by way of subsidy of $ 5.46 instead of riding boots, skullcaps and safety vest and each employee must provide a suitable skullcap, safety vest and riding boots as required.

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APPENDIX 2

A.T.A. Recommended Training Fees

The ATA has reviewed recommended training rates as a result of new Wage Rates effective **1 July 2014** for the Horse & Greyhound Training Award 2010 (HGTA).

Members should consider reviewing their training rates as a result and adjust accordingly if required. **(Please note amounts below are per day & exclusive of GST)**

New South Wales	**$123.30**
South Australia	**$107.80**
Victoria	**$119.75**
Queensland	**$116.25**
Tasmania	**$105.10**
Western Australia	**$112.00**

For further information contact:
Australian Trainers' Association
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A.T.A. Recommended Race Day Attendance Fees

This table of fees are a guide only to recover costs (**billed to owners**) associated with attendance at race meetings by stablehands, in accordance with the Horse & Greyhound Training Award 2010 (HGTA). The ATA's recommended race day attendance fees are based on 3 ordinary hours of work.

Race meetings Monday to Saturday	**$115**
Race meetings Public Holiday, Sunday & Night	**$160**

Racecourse Attendance Allowance for Employees

Every employee who is required to attend a race meeting must be paid a Racecourse Attendance Allowance under the Horse & Greyhound Training Award 2010. Please see overleaf for the current rates that apply.

For example, should an employee attend a race meeting 120km from their place of employment then the employee is entitled to a Racecourse Attendance Allowance as follows:

First 75 km $23.70 plus $5.58 for each 50 km (or part thereof) after 75km. Therefore based on 120km of travel, the Racecourse Attendance Allowance would total $29.28 in this example.

Please note - The Award provides that when required to attend a race meeting an employee must be paid an allowance of $10.77 for each meal unless the employer supplies the meal.

WAGE RATES EMPLOYEES

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RACECOURSE ATTENDANCE ALLOWANCE

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ATA RECOMMENDED TRAINING FEES AND RACE DAY ATTENDANCE FEES

Effective 1 JULY 2014