18 November 2009

RESPONSE TO THE
PRODUCTIVITY COMMISSION DRAFT REPORT ON GAMBLING

ABOUT THE TASK

As I feared at the outset, this exercise has gone off the rails, at least in respect to racing. The result is not up to the Commission's usual high standard.

By far the biggest diversion occurs because the Commission has not stopped at the racing station and instead has gone down an offshoot and pulled up at the wagering station. Even then, it has concentrated on only one or two platforms at the expense of others.

Another part of the problem is that the English language is being clobbered. Here the Minister's brief did not help.

The generic term "gambling" is far too loose. But if you use more common definitions some differences quickly emerge:

- Gambling involves a chance event – ie it's impossible to predict.
- Punting or wagering involves an assessment of the options, followed by a considered choice – ie a degree of predictability is involved.

Products and services may cater for people in both groups but to confuse the two terms is to risk making bad judgements.

Gambling may incolve betting on races but only when the investor has no idea of what he is buying (eg Mystery bets or using a pin to select a runner). By definition, punting can never be gambling in that sense because it involves known factors and their interpretation.

The Minister's reference does not talk about racing or punting as such. However, let's assume that the Minister intended to cover punting on races. Certainly the Commission read it that way, although it has not handled the subject in sufficient depth or breadth.

In practice, the reference should have been split into two completely separate areas: problem gambling on the one hand and racing and wagering on the other. The former has been more or less completed, the latter barely touched. Indeed, wagering cannot be addressed properly unless you first evaluate racing as an industry.

The attached more detailed comments are offered with the above provisos. I hope the Commission has enough time left to do the subject justice.

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WHAT REALLY MATTERS

- The report is papering over cracks in the ceiling while the building is falling down. It brief on racing needs to be clarified and expanded.

- Wagering is not *an* industry but merely one sector of the racing industry

- The racing industry will one day realise it owes the NT bookmakers a debt of gratitude for stirring the pot. Meantime, the important thing is to understand how they got there.

- The case for paying commission or fees on the basis of bookmakers' gross revenue is weak and is based on too narrow an outlook.

- More importantly, over time the existing gross revenue package is unlikely to permit the industry to flourish. The Commission talks about free riding but cheap riding is nearly as bad.

- The Commission addresses consumer interests as they apply to a small minority yet skates over the interests of the majority.

- Racing's owners and managers (whoever they all are) are entitled to, and need to, set fees and commissions. Bookmakers, effectively acting as selling agents, may express firm views but have no such rights.

- Organisationally, the racing industry is fragmented and ineffective and is incapable of achieving optimal growth in its present form.

- The industry cannot settle down into a growth mode unless and until state governments and racing administrations adopt a more enlightened approach.

- The industry is overdue for major structural reform, and therefore for a realignment of its betting opportunities.

COMMENT ON DRAFT REPORT

Background Matters

I appreciate the considerable efforts by the Commission's administration to keep the review tidy and timely and to keep the public well informed. A job well done.

I have some concern that the Commission's resources may have been wearing out by the time it got to wagering. One chapter out of sixteen is not much for one of Australia's largest industries. Sixteen and a half of the seventeen Key Points concern gaming only, most of it problem gaming. Hence, perhaps, a lack of consideration of how and why the racing industry got into its present mess.

Maximising What/How?

Draft recommendation 13.1 includes the Commission's central objective of "maximising long-term consumer interests". So what does that mean?

Picking your way through the report uncovers two key items which help explain it. One is the broad concept of enhancing – or "maximising"– competition amongst betting operators. The more the merrier. That will keep prices down.

The other is the availability of more attractive prices as a function of the lower cost base that NT bookmakers enjoy and the lower takeout fees they and Betfair are demanding for the future. These things justify their precedence in the Commission's league table.

Even if this argument succeeds, it leaves open the question of what sort of industry the "maximised" consumers will be enjoying. The same? Worse? Better? We can have no real idea of the answers there as the report has failed to address a range of potential future industry structures or scenarios. The chances are that they will be different to those applying today.

Let's remember that the current instability emerged only because of the racing establishment's ineffectual handling of the bookmaking sector. The differences were magnified by radical change in technology in recent years but that was not the root cause.

Will this process not continue? And will not state governments continue to modify their regulations as time passes? They certainly have in the past. And since they will almost certainly be losing tax revenue they will be very keen to act.

As those future events are unknown, it is entirely possible that consumer interests may not be helped by the Commission's proposals.

As I explain later, one scenario would change the industry for the worse. Were the low takeout fees to persist, some or all of the traditional sector would be forced to follow suit, thereby reducing industry income and endangering its viability or at least causing major restructuring.

In this context, a short term maximisation could easily result in a long term degradation of consumer interests. What if you had a great betting setup but nothing to bet on?

Incidentally, were the NSW courts to “approve” the NT bookmakers’ right to set their own fees, what would be the next step? The court is not going to rule on the amount (it is not a prices tribunal), only on the correctness of the system. So, in future, will the bookies reduce them further, knowing the hold the whip hand legally? Or even increase them if they feel like it? The industry could become a complete shambles. For this and other reasons I will be astonished if they win their case. Similarly, Andrew Twait of Betfair makes a song and dance about how paying a 1.5% fee on turnover would put him in an unfair competitive position – yet he says not a word about changing his basic takeout rate from 5% to something else. What is so sacred about the 5%?

The only reliable scenario in terms of consumer interests is an industry which has underlying strength, which is commercially oriented and well managed and is therefore flourishing. The Commission’s proposals not only do not achieve that end, they do even address it. That error has occurred because the Commission looked at wagering as an industry, which it is not, and generally ignored racing, which is.

Regulating Wagering

A national body? The Commission’s prime recommendations require all nine states and territories to agree to transfer power to the Commonwealth. After looking through the formguide (and it’s quite lengthy), a kindly bookie might offer 100/1 about that possibility. Air navigation is one thing but playing around with state tax revenue quite another. Even COAG agreements on competition are probably honoured more in the breach than in the observance – well illustrated by TABs themselves.

Indeed, for topical interest, here’s what *The Australian* (18 Nov 2009) said about the Crawford reform proposals for merging state and federal Institutes of Sport: “However such a proposal would have to win the backing of all state governments in the Council of Australian Governments (COAG) forum, a prospect that some sports leaders think is unlikely given the history of disagreement between them”.

Or as Crawford is quoted: “The current complex and competitive system is one of the greatest inefficiencies in delivering elite success on the world stage’. And, “The duplication which is inherent in the state/territory focus is now one of our greatest opportunities for reform”.

The next option might be for those same governments to reach an administrative agreement about the same things. That might cut the odds down to 25/1 or even less but it would leave us with a messy and argumentative structure, and subject to political interference.

Even if everyone eventually agreed, it would take considerable time and effort to produce workable objectives and ground rules for the new body. Some years would probably pass before the first decision was made about commission rates.

We need a Plan B.

Logically, that would be an advisory panel (perhaps as an added function to an existing role) which would operate in much the same way as a permanent body. It might even illustrate to state governments (and me) the benefits of having a permanent body in the future. While they could easily do it, Racing Ministers will need lots of encouragement to go down this road.

Even better would be a strong and progressive industry management which could do its own thing, subject only to intervention in the event that a gross bias or inefficiency is present. (Such a process is not a long way from several in operation today).

Separately, there is no reason why all the states could not approve a national betting pool. It's not too controversial and it would help the industry and many of its customers, remove many anomalies and even level the playing field a bit (NT bookies would no longer have "best tote" odds to push). They have been urged to do this more than once (by Tabcorp, the Cameron review and former Racing Minister Face, for a start) but with little response so far. This is a straightforward administrative matter which requires only some programming work by the TABs. And it would provide a modest guide to bigger and better things at the national level.

In all likelihood, none of the above discussion would have been necessary had the racing industry and governments adopted normal commercial behaviour and principles in the first place. Heavens, they could even do that today!

Priorities Confused

The report regularly implies that wagering is a stand-alone industry and discusses it only in respect to benefits for its direct consumers. This is dangerous and misleading. Wagering is no more than one of several services supplied to the racing industry. A large and vital one, certainly, but still just a subsidiary service.

Were wagering to disappear, racing would still exist. A bit bleak, of course, but it would still exist. But the reverse does not apply. No racing means little or no wagering. Sports, elections and flies on the wall could hardly sustain the sector as it stands today.

Wagering has to fit into racing, not the other way round. By all means examine wagering's good and bad points, but always with an eye open to its impact on racing. The parts cannot be separated from the whole. And it is the whole that must retain primacy. Productivity emerges from an industry, not from an industry sector.

This situation contrasts with gaming/EGMs which can operate independently of the host which runs them. At Las Vegas airport, for example, you can try your luck on the way to boarding the plane.

As I tried to point out in my original submission, gamblers are just gamblers but punters are first and foremost consumers of racing.

Finally, the term “corporate bookmaker” is a nonsense and it is disappointing that the Commission accepted the racing establishment’s corporate spin to this effect. NT bookmakers are no different to ordinary bookmakers (many of whom are now incorporated); indeed, they are usually the same people and some still maintain traditional bookmaking operations in home states. This distinction, which possibly dates from the days when bookmakers were compelled to be sole traders (regulation again!), is not a semantic one as it colours attitudes and analyses unnecessarily.

The Root Cause of all Evil

It is a little incongruous that the Commission recommends additional regulation and another regulatory body when intrusive regulation is patently one reason for the industry’s poor financial performance in the past. In contrast, the Commission makes no comment on the need for or the possibility of reducing regulation, which means inefficiency will persist, no matter what else happens.

Major Proposals

The Commission has put forward two key proposals to sort out topical wagering problems:

1. Create an independent national body to decide on commission rates.
2. Charge on the basis of the wagering operator’s gross revenue – ie the surplus of wagers over payouts (but not for TABs, apparently).

The first point is theoretically workable, although I have qualms about a producer being ordered to charge a particular fee. Such a big brother approach pre-supposes that the public have unusual rights and therefore need extra protection. The former is not really a killer point while the latter is accomplished at least partly by the stewardship function in all racing codes. The underlying issue is that state treasurers want to keep their fingers on the till.

The Commission should also address the point that decisions of such a body could radically change the nature of the entire industry, potentially more so than implied in the draft report.

On the other hand, there must be considerable doubt about the second recommendation. The supporting evidence offered is either weak, circumstantial or inappropriate.

Several points seem relevant here – not only in respect to fees but to the industry more generally …

1. The Commission is suggesting the tail should wag the dog. The selling agent’s profitability is seen as superior to the profitability of the industry as a whole. Superior for customers, we assume? Surely the dominant influence on any fees should always come from the owner/producer, subject to reasonable equity and fairness. It’s what he charges to enter the arena. This is not to fix ultimate selling prices but to ensure the producer

gets the cash he sees as necessary to progress his business (which is barely happening at the moment).

2. A flourishing industry will generate more attractive opportunities for all participants, including betting operators. Any currently popular sector of that industry with a particular business model – NT bookmaking, for example - can change overnight, whereas industry profitability needs to be reasonably predictable.
3. Offering company tax collection methods as a parallel is quite ridiculous. Does the Commission suggest a bookmaker's annual loss should permit him to make deductions from future years' fee payments? Besides, the tax man works on nett revenue, not gross revenue. The clause should be removed from the report.
4. It is not clear why an individual bookmaker's day-to-day effectiveness (or good luck) should affect the price he pays for rights to an input service such as field lists. In contrast, the use of turnover is simple, definitive, consistent and indisputable. How the wagering operator works under that requirement is up to him. It is not up to the producer to modify his need to suit any particular operator. Nor is it up to regulators to pick winners – the market will do that without any help.
5. A number of examples used by the Commission to "justify" charging on gross revenue are irrelevant or misleading. In most sports, and unlike racing, the currency is not a dollar but a point won or a run scored. Such arrangements as have been concluded with those sports are no more than bilateral commercial agreements which happened to satisfy both parties in <u>their</u> circumstances. They were created when a betting operator walked up to a sport (which had nothing) and asked, "Would you like some money?" Were they going to argue the toss? Hardly. In any event those sports are not dependent on such fees for their viability, as racing is. No particular justification exists for its transfer to racing.
6. Further to the last point, the presence of betting operators on a sport's sideline has no effect, as such, on the structure and overall efficiency of that activity (assuming normal protection against abuses are in place). In contrast, betting is integral to the operation, structure, survival and progress of racing. Chalk and cheese.
7. Comparisons with other countries are odious, at least unless complete packages are included in each case. Even then, they are dicey because the playing fields are different.
8. According to the Commission, the gross revenue approach favours small and/or more operators, which it considers a good thing. That point is itself arguable. Regulation should not decide who plays the game.
9. The numerical evidence put to the Commission is no more than a record of past practices, good and bad. Its use implies the material is helpful even though it emerged from an artificial construct – ie from a highly regulated, highly conservative and highly introverted industry. Like the TAB takeout, these figures should be treated as arbitrary. They have no intrinsic validity except as a record of the past.
10. Producing a few Greek symbols does not make a case. Why should the producer be responsible for the agent's profitability or his business model? The producer cannot tell the agent how to go about selling his services,

who to hire, what sort of bets to accept, which customers he should favour over others. Doubly so in such a volatile and emotional activity.

11. The Commission concludes that encouraging low takeout operators is not only a better strategy (which is reasonable up to a point), but that those operators' particular takeout rates are desirable, or even set in concrete, simply because they are lower at the moment. That is a heroic assumption and hardly justified as such, particularly in view of the artificiality of the industry's structure.
12. In total, the Commission has classified cheap rates as best rates. Yet the newcomers are simply trying to exploit processes that are better for them in today's circumstances. That's natural enough. But does it help the industry at large? The evidence says not, or not yet. This is where the biggest danger lies.

Worrying about the detail has left a much bigger gap. The Commission does not address the real reasons for the failure of the industry to flourish over the last two decades, or the impact of such failure on the success of individual sectors or on wagering itself. The evidence shows that the prime influences have been over-regulation and the continuing poor management and ineffectual organisational structure of part or all of the industry. Therefore the Commission has left the buck floating around in the ether.

Indeed, the key question about virtually everything on this subject is … who runs racing?

By way of background to that subject, let's note that WA's ill-advised and poorly researched attempt to outlaw Betfair could have been motivated by no other factor than emotion (Betfair had always offered to pay fees). Until that time the chief of the ARB, an outspoken opponent of the Betfair concept, was a Perth resident, while I am aware that other local racing people were opposed to Betfair.

Leaving aside Betfair for the moment (it's a totally different product and may well justify different treatment), the current kerfuffle is due to nothing more than a handful of bookmakers moving away from home and setting up shop under more favourable conditions. It's a very straightforward matter to digest.

Businesses or even individuals do that every day, quite often encouraged by bribes from state Premiers which end up costing taxpayers a lot of money – something the Commission has reported on unfavourably in the past. Indeed, that is precisely what the NT government has done for bookmakers. One obvious effect is to transfer tax revenue from other states to the NT.

The critical question then is: what would have happened had governments and industry created more favourable conditions in those home locations? Clearly, you must conclude that the product range would have widened, betting turnover would have increased and consumers would have been happier. All of which, arguably, would have produced higher prize money, higher attendances and more tax revenue. How much more is a moot point.

There has been no historical problem with turnover-based fees for bookmakers, nor any question of their suitability. The subject arises only because NT bookmakers are trying to pay less and have devised a plan which helps their objective. Curiously, every single one of the NT bookies has been, and most still are, paying commission on turnover in their home state. No significant campaign has ever been mounted to alter those systems.

There is a problem with TAB takeout levels but there the decisions were made arbitrarily by governments. Hopefully, a future structure will see competition exert a downward influence. At the same time, there is no reason that any minority – in this case, NT bookmakers – could not adjust to the same basic system.

It is likely that such a "home" scenario – by virtue of the larger pie – would also have enhanced TAB turnover, not just that of the bookmaking sector.

Future Effects

The fact that the above (more desirable) process did not occur must be sheeted home to a combination of state government policies and decisions by racing authorities, which themselves are often intertwined. It is those two areas which demand more forensic treatment.

At the very least, that process would (or should) affect the nature of the Commission's recommendations. In any event, it is surprising that the Commission has not seriously ventured into industry organisational matters. That shortcoming not only affects its recommendations but bypasses the need to encourage a more efficient and effective future environment (eg one where frustrated groups were not forced to revolt).

Equally, it is surprising the Commission does not significantly address the monopoly rents charged by various TABs. The fact that these are underpinned by state legislation does not make them right or optimal – quite the reverse, really. Consequently, punters are subsidising TAB executives and shareholders.

Doing nothing more than changing a few numbers may serve only to build a future of a slightly different shape but with the same old problems.

While I am not able to comment on gaming subjects as such, it is necessary to note that the majority of EGMs are under the control of not-for-profit organisations, just as racing is. The licensed club industry, which also plays a large role in ClubTAB operations, is characterised by frequent mergers, financial collapses and reducing member services. As a long time social club and raceclub patron, I have yet to see one in which I would be prepared to buy shares.

The differences between social club or raceclub management practices and those of the general corporate community are massive. One should always look twice at the actions of an unpaid manager – or, more precisely, the actions of a management committee. They are often not rational, or not in the conventional sense.

"Low Price" Operators

Some aspects of the Commission's conclusions may be challenged (see p13.31).

First, a direct comparison between "low price" and apparently "high price" operators is argumentative as they either operate in different circumstances (NT or traditional bookmakers) or offer a different style of service (TABs and Betfair). The overall value of any service may be measured in ways other than cash. By comparison, some consumers want the style of service offered by David Jones or Myer while others are happy with similar goods displayed in a dusty warehouse.

To arrive at its recommendations the Commission has assumed the current regime will continue. Why so? Surely the Commission must at least be looking at alternative scenarios, including those where one or more southern state governments adopt a more progressive regulatory approach. Things like regulations, takeout rates, profitability, customer incentives and the like can and do change at a moment's notice.

Further, the Commission makes much of the consumer advantages which accrue from lower rates – indeed, that is central to its major recommendations. However, that covers only the minority who are dealing with the NT. What of the majority of consumers, including those who do not want to or cannot take advantage of the NT services for whatever reason? By definition, they will be less well off as time passes, even assuming some transfer of low costs from the NT to the rest of the country. How does the Commission intend to balance the competing consumer interests – ones involving the majority?

Point One: The Commission must address the southern state governments' justification for any or excessive regulation.

Secondly, the Commission appears to want to protect low-price operators and underwrite their business models purely because they look good today. Yet there is no guarantee that those or any rates will continue (and any likely national rate-setting is possibly years away, if it comes about at all), nor any reliable assessment of what the future environment will look like. Indeed, one scenario (which has significant advantages) would have it that they will be paying somewhat higher fees.

Additionally, the bare rate as such does not cover other incentives (ending up as costs) which operators may and do bring into play. Funding such incentives is possible mainly because of the NT bookmakers' low cost base. That's nice in a narrow sense but is it sustainable or desirable in the long run?

Another anomaly is that the Commission suggests that a new national body should develop fixed rates while at the same time it applauds competitive behaviour which leads to lower or varying rates. The two cannot co-exist.

Point Two: Surely the Commission's major task should be to recommend a desirable environment. Having done that it may then wish to go into more detail about some aspects of the industry. At the moment the cart seems to have got in front of the horse.

The Commission appears to accept that "the capacity for corporate bookmakers to trade at higher prices is limited". Why is this true? Or is it true a slightly higher rate, a moderately higher rate or a much higher rate? This is not a linear equation so we don't know the practical answers to those questions and it is therefore hasty to base future policy on any such assumption.

It is as well to remember that NT bookmakers have a wide range of customer types, from $10 punters to those who bet $1 million at a time, from mums and dads to crooks (literally). Indeed, I believe $5 million has been the maximum (the bookie won!). Clearly, the bookmaker will be negotiating rates for such bets with the customer. Inevitably there will be some interaction between price discounts and fees paid (under a gross revenue system). In effect, the bookmakers' bet-to-bet practices, where their successes will be variable, would influence their gross revenue figures at the end of the day and therefore the amount of fees paid.

As a matter of interest, had the bookie lost that $5m bet, he would have paid no fees that day under the Commission's favoured scenario, whether on that bet or the myriad of other smaller bets he would have taken. Is that realistic?

Point Three: Considerable research would be required before suggesting whether any particular rate is good, bad or indifferent in a variety of circumstances. Such study has not occurred (or not in public anyway).

It is stated (more likely just asserted) that NT bookmakers have a market that "would not exist at >16%". Perhaps, but so what? Here we are delving into the practices and the psychology of punters, especially large or well educated ones. However, the Commission should start off its thinking with the assumption that no normal punter could exist (profitably) if he was routinely paying out 16% to any wagering operator. In the event that the punter is nominally paying that much he must then seek a runner priced well above true odds – which is what most punters try to do every day. If they fail they will go broke. Alternatively, if he enjoying a lower takeout rate then he can be more flexible about the runner's pricing.

The first law of punting is that both parties must have a chance of winning. In today's circumstances that is not always true. See below.

Point Four: To better understand this and other points the Commission would do well to develop profiles of (a) the average mug gambler (on racing), (b) the average serious recreational punter and (c) the average professional punter. After all, these groups will react differently and are treated quite differently by bookmakers and TABs, so why not by regulators and analysts, too?

TAB Comparisons

Also note that TABs typically charge more than their normal rates when framing Fixed Odds prices. This is a belt and braces approach to what amounts to bookmaking.

Further, note that the TAB business model includes bets attractive only to mug gamblers. Some of these not only have high takeout rates but the style of bet makes it impossible to win anyway. For example, a boxed Trifecta of three runners (contained in a standard Mystery bet) is a mathematically guaranteed loser*, just like the poker machine, even at zero takeout. Rather than the nominal 20% or so, the TAB picks up perhaps 30% or more of the investment. (Note: the increasing popularity of such Trifectas has already ruined their potential value for serious punters – ie enough successful Mysteries are bought to reduce the actual dividend to below "true" levels in many cases. It is little wonder that NT bookies are now happy to take Trifecta bets).

**Virtually by definition (and also by TAB runner selection policy), any three runners will be quoted at different prices – ie with different chances – yet the Mystery bet treats them as all having the same chance. The TAB has won before the race starts. This syndrome is exacerbated by numerous poorly qualified tipsters (many sponsored by TABs and racing authorities) who regularly recommend "boxed" bets to the public.*

Point Five: For these and related reasons, the quoted Credit Suisse claim is pretty much irrelevant.

Point Six: The implication that much or all of the NT bookmaker market is attracted only by low rates/favourable prices ignores many other probable reasons – convenience, accessibility, timing, bet size, and a generally better product range than that offered by TABs or traditional bookmakers. As with most products, price is not the only factor. Of course, the same might be said of traditional bookmakers, too.

A Risky Conclusion

The Commission's conclusion (13.31) is suspect and may be unfair in itself. It claims:

> "… turnover-based fees will tend to either drive low margin operators out of business or compel them to change their business models and increase their prices to punters. In short, turnover based fees discourage price competition between firms."

This can be no more than one of many possibilities, and one of the most unlikely. On the first point, the Commission can have little idea of what such operators would do in a variety of circumstances – perhaps they may not know themselves. However, the essence of this argument is that if NT bookmakers pay the same fees as southern bookmakers they will go broke, even though they are paying lower state taxes. Hardly an acceptable proposition.

Further, the prime motivations for the establishment of the NT bookmaking sector were the regulatory barriers down south which stopped them from doing business when, how and where they desired. Lower NT taxes simply made their operations more profitable. Industry fees are just another part of the same discussion.

On the second point, such a blatant statement is not warranted when the full circumstances of any future environment are not known. Indeed, there would be some doubt that complete competition exists within the NT group itself today, given that they are all furiously promoting "best tote" odds, including via expensive TV ads.

That is, amongst other options, they all have an identical product, which is at odds with the normal competitive behaviour within a group of bookmakers.

In any event, the theory that fees and competition are linked is not proven or plausible. If all fees were the same then operators would find other means of competing – on price or service – as they have been doing for more than a century. The Commission misses the point that bookmakers and their customers are invariably price-sensitive, whatever their overhead costs may be.

The Commission is effectively saying that NT bookmakers are stronger competitors because they have lower overheads and are bidding to pay smaller fees than other operators. This is not particularly logical. You are not a ‘better’ competitor simply because one government gives you a free kick and another does not. Especially not when those governments can change the rules at the drop of a hat.

In general, traditional racing is being asked to change its business model, leaving NT operators to do as they wish. So the principal is wrong, the selling agent is right? OK, there is a grain of truth in this at the moment but it is highly likely the playing field will change as time passes (and so it must, as discussed below).

The underlying assumption – a reasonable one - is that traditional fees are too high and that competition would bring them down or keep them down. That should happen, of course, in the interests of a bigger betting pie and increased efficiency. However, to underwrite the current NT model, including the gross revenue option, is to suggest that traditional operators will have no choice but to change to that system, too. As time passes, that would result in average commission per betting dollar decreasing substantially. The eventual outcome may be that overall racing industry income-per-unit would decline, even if a useful increase in total wagering were to occur (ie due to a more attractive product range).

While some such reduction may well be absorbed by increased efficiency, it is more than likely that it would also cause overall service and product quality to decline.

In short, using “gross profit” at current rates across the board is unlikely to be sufficient to sustain the industry. The resultant income decrease would cause a lowering of prize money (which has already happened on a temporary basis), impact severely on the breeding sector, put an already shaky owner group into an even greater loss area and pull cash away from needed public facilities and services. Does the Commission suggest these are good things or that they should be ignored?

(It should be noted that racing has only two substantial financial inputs – capital invested by owners of racing stock and betting. Yet, on average, owners never recover even the major portion of their investment. They continue for emotional reasons: the hope of windfall gains, the prestige and the enjoyment and excitement of chasing the elusive win. TV footage of owners post-race tells the story emphatically).

In any event, it would be very difficult to bring that about that homogenisation, not only because of various government attitudes but because there is unlikely to be enough money left (in commissions) to run the industry effectively.

But take it a step further. If the practice were to apply universally, the hard truth would eventually emerge. To allow the industry to prosper or even survive, “gross profit” style fees would have to increase significantly for everyone, which suggests that, over time, we would turn full circle, but might be left with serious imbalances in the system.

The point surely is that both the traditional sector and the newcomers are failing to optimise gains for the industry as a whole. Both must change to achieve stability and efficiency.

While the Commission fears driving NT operators out of business (an unlikely possibility), the other alternative is to drive traditional bookmakers out of business, which is already happening to some extent, and to risk making TABs much less efficient and less accessible. Much as I would like to see the TABs cleaned up this is not the way to do it. In either event, many consumers would lose out.

On the ground of equity alone, a solution somewhere between all of these is probably ideal.

However, consider a further scenario: Suppose NT bookmakers pay the same fees as everyone else but continue to receive the local cheap tax rate. Now there is a continuing imbalance in the industry favouring the NT people and southern operators will be wondering how on earth they can compete. That would pose a serious management problem for the industry. The only way out of that conundrum would be a nationwide agreement between states and territories to charge common taxes. A daunting proposition, but it is just one of several possible outcomes!

Industry Control

However, a further point is relevant. The essence of the Commission’s recommendations is to let NT bookmakers rule the roost and effectively set their own rates. This leaves racing management out in the cold, unable to sufficiently influence its own destiny. Such an approach emerges partly because the Commission is treating wagering as a stand-alone industry in its own right. Of course, that is a nonsense as wagering exists only because races are offered. (Preferably they should be good races – ie attractive to punters – but other measures are better suited to achieving that objective).

Racing’s controllers, or the racing’s industry’s owners if you like, must be entitled to set a fee level, subject to oversight as to reasonable equity and fairness. No one sector of the industry is entitled to that same privilege, whether bookmakers, owners, trainers, customers, formguide producers or pie sellers. Indeed, you might include governments in that group as they have a poor success rate when they intervene.

Some years ago, the NSW Treasury imposed an increase of 0.5 points in the TAB Win takeout rate, whereupon millions of betting dollars disappeared overnight down the Hume Highway to Victoria. Treasury changed its mind a couple of months later.

Generally speaking, the market will tell the industry whether its rates are desirable or not – or it will if the industry is listening. (While I agree with the Commission’s point that wagering's massive decline in market share suggests a level of dissatisfaction is present, that may not be the only reason. For example, increased availability and convenience of EGMs is a factor. So is the decreasing level of education about racing and punting – itself a product of non-attendances at racetracks. And so on. That is, the gambling industry has done better and racing industry has done worse).

Funnily enough, for years after their inception TABs were formally regarded as no more than a service to the industry. Oncourse totes were mostly run by private companies which contracted (competitively) to raceclubs and pooled bets with the TABs. Only in more recent years have TABs bought out those oncourse operators. Indeed, later on, governments sought industry approval and paid hefty bonuses to the industry before concluding TAB sale agreements. That is, they specifically regarded betting operations to be the child of the racing industry.

Today, such a pecking order still applies in theory but not in practice. Leaving aside NT bookmakers, the TABs now effectively control the show in every respect except the actual running of the race. No doubt it is the potential loss of that control which is producing most consternation in TAB boardrooms or amongst racing authorities, and which prompted Tabcorp to establish its NT bookmaking operation. (Note also the extraordinary plea by Tabcorp's boss to the NSW government to ban betting exchanges at the time the Cameron review was being organised. This astonishing political naivete – the Premier's riding instructions were already obvious - throws further light on the castles TABs had been building with the help of a one-eyed racing establishment).

Eventually, in part or whole, the proposed national body would have to keep an eye on all this. But will it happen? And can we afford the wait?

The Supporting Data

Going through the interim report I get the impression that the Commission is concentrating more on being a referee than an analyst or innovator. Certainly, most of the recommendations are fairly clear but some of the reasoning is not. Economic principles are all very fine, but they must be considered in the light of the environments in which they work, and they must be applied widely.

In many areas I see an acceptance of data at face value. But more critical are the factors that generated that data. For example, a decline in real wagering is noted but there is not much about the reasons for it. Since that is the industry's lifeblood, it warrants more thorough treatment

Then, over time, racing management has taken or omitted to take some steps but the reasons for their actions are investigated only superficially or not at all. For example, why did racing management (and governments) take a negative approach to bookmaking as such and what would have been the outcome had they not done that?

The Commission plucks out occasional references to the UK position yet there the bookmaking sector has always been the dominant force, including via suburban shopfronts. That makes it difficult to compare directly with Australia. Then in the US the tote has always been dominant, but with extraordinarily high and variable takeout rates (and hence a history of illegal bookmaking activity), fluctuating policies from state to state and, more recently, some track closures (usually blamed on competing casinos, many of which are on Native American reservations with their attendant tax advantages). In any event, comparisons between countries are odious, at least unless you compare complete packages.

(It is interesting to note that some of the UK competitors in the Melbourne Cup, despite having several well regarded wins, arrived with prize money totals that barely equalled those of run-of-the-mill local gallopers – ie around $200,000 or so. This suggests UK prize money levels are not great and that Australian cash was far more attractive to them).

In other words, wherever you go, the industry is an artificial construct in many ways. Australia features heavy but not always effective regulation, a tendency to disregard consumer wishes and questionable organisational practices. To say nothing about its defensiveness, its introversion, its frequent rudeness (parasites and plunderers?) or (as the Federal judge stated about Racing NSW) its lack of professionalism. And, of course, its strategic planning appears non-existent. The industry operates in a permanent 12-month survival mode, much like the local tennis club. Belatedly, and seeing their poor capital structure and risky income streams, many clubs are now frantically looking to diversify into non-racing ventures.

Given that artificiality, nothing in racing's history can be taken at face value. You have to turn over the rock to see what's underneath.

Whose Figures are Those?

An impression is created that the nominated takeout rates used by NT bookmakers and Betfair are gospel. But why should that be so?

Bookmakers set those rates themselves, with reference only to what would suit them best. But to say these are ideal rates implies that if Harvey Norman discounts a TV set then that new price is the "correct" one. Not so, of course. It is simply what Harvey Norman wants to do for its own internal reasons. Next week, it may do something different.

Betfair is little different in that it is a unique product and prices set by customers may or may not compare logically with other market prices. Betfair customers may well be prepared to seek more or less in the bargaining process, as they value certain aspects of the service differently.

Further, should Betfair (be forced to) increase its takeout rate to accommodate higher fees then its customer base may well be affected. Or it may not, depending on other market conditions – which are hard to predict here. Certainly the 5% works well in the UK and has proved popular here. But that does not mean that a business model using 4.5% or 5.5% would not work just as well. All that aside, there is some justification for Betfair to be charged differently as it is a genuinely different product to that offered by bookmakers or TABs.

Finally, some sources quote supposedly actual or potential diversions of business to NT bookmakers or Betfair, primarily from southern TABs. There is no proof of these figures, or none is offered, so they must be considered no more than assertions to suit the message of the day. Equally, no evidence is offered as to whether the Betfair service actually generated new activity, even new customers – which is quite likely.

In any event, accuracy would be hard to achieve in this area. To get reasonably close to the truth it would be necessary to conduct in-depth interviews and analyses of a large number of punters' habits and actions. Is your NT/Betfair bet in addition to what you usually do (ie down south) or instead of? Are you still betting as much, less or more with your usual TAB? Has the size of your bet increased due to perceived greater attractiveness of the alternative product? If so, what particular products are better than others? Has your annual betting turnover varied over, say, the last five years? If so, how and why? And so on.

There is no evidence that such studies have ever been conducted, which suggests any evidence is pure anecdotal. Consequently, related claims on this subject from contributors should be disregarded. Back of envelope stuff and guesstimations are not worth a cracker.

Management Practices

To suggest that the decline in traditional wagering's slice of the gambling pie is a function of the arrival of newcomers or some other external factor is ingenuous at best. Rather the evidence shows it is in good part a function of the competence of racing management and its general desire to avoid change and "do what we have always done". And the industry has plenty of form. For example …

- Management discriminated illegally – eg refusing a trainer's license to Gai Waterhouse because she was a woman.
- Raceclubs have previously had bans on women becoming members, or on joining the committee.
- Management once refused to allow phones on course or to free up access to them for bookmakers and others. Even public phones were banned.
- Management refused to provide more incentive to traditional bookmakers or even to allow them a level playing field.
- Management effectively ignored the rise in popularity of offshore bookmaking firms and the reasons for the implied diversion of business.
- Management aggressively attempted to make illegal the operations of NT bookmakers despite obvious consumer wishes.
- Management (initially) refused to deal at all with NT bookmakers.
- Management subsequently refused to negotiate with bookmakers, as did the NSW government.
- Management refused to allow a big punter to access Betfair oncourse.
- Management aggressively fought the arrival and/or legalisation of betting exchanges despite the clear desire of customers to patronise them.
- Management strongly petitioned the Commonwealth to ban betting exchanges when it must have known that would be difficult politically and legally (and major raceclubs abound with legal eagles).

- Management failed to address the need to better educate and attract prospective new customers, despite the continuing decline in attendances. (I discount the sometimes significant efforts to attract the social set to champagne-fuelled marquees and the like. These folk probably don't bet much anyway and they attend only carnival days).

This overwhelmingly negative, conservative, stick-in-the-mud philosophy radically affected racing's income as customers drifted away from traditional betting media to more interesting outlets or away from racing altogether (eg to the latest fad – poker).

Racing was always comfortable with the goose and the golden egg but forgot about ducks, turkeys and foxes.

That same trend was exacerbated by the arrival of SKY broadcasts and the perceived greater attraction or convenience of betting in handier off-course locations and, more recently, by the TABs' concentration on "mug" gamblers via such things as Mystery bets, Duet bets (which surely cannot recover administration costs), hot tips and the like.

Note that the introduction of SKY coverage to a racetrack always induced a jump in turnover, indicating that viewers were then more inclined to bet. While that increase was sustained it does not appear that the upward trend continued. It was a once-off boost – something that NT bookmakers might keep in mind. It also implies that interest in racing had already reached its peak under the prevailing conditions (which is why some jurisdictions or clubs are canvassing the option of establishing poker machine palaces oncourse. Indeed, several have done so already but apparently with mixed success).

The concept that racing's fortunes are tied up with the rapid growth in turnover being diverted to, or generated by, the NT bookmaker group in the current decade is somewhat misleading. That drift started long before their establishment as a group, primarily as bookmakers became disenchanted with operating restrictions – viz Mark Read's warning in 1992, CentreBet's formation in the same year and the 1990s popularity of offshore bookmakers in Vanuatu and later Fiji and Norfolk Island.

These basic signs of market dissatisfaction were either ignored or their impact on conventional business disregarded. Hand wringing or chardonnay lunches (as Quimby QC noted at the time of his "jockeytapes" investigation) were more popular than corrective action. Such is the nature of the management of racing.

Let us note here that there is no such thing as "a" manager of any racing unit – whether club or authority. The management function always falls to a committee appointed by members or governments respectively.

Consequently, slow or no decision-making, a concentration on bureaucratic processes (as qangos, racing authorities must conform to numerous public service requirements), maintenance of the status quo and short vision characterise the industry's operation. Innovation and change are avoided and initiative is discouraged. Shortcomings are swept under the carpet.

That committee members of raceclubs are insiders is axiomatic. However, so is the membership of some state authorities – in obedience to the common ministerial policy of “encouraging the industry to run itself”* (and, similarly, the laughable claim that ministers want to be at arms length from any matters within the authority’s responsibility). Exceptions are few, or are limited to the occasional individual – for example, SA Greyhound racing is run by an independent group, while Tasmanian racing is under the care of the government-owned TAB, and therefore of its racing Minister.

** This somewhat obsolete practice has done little good for grower boards of various sorts and many have since discarded it. The Wool Board, for example, has been a constant source of dissention and dubious business policies, despite a couple of cleanouts over the last two decades. Wool’s share of the world fabric market declined from around 20% to under 2% today, part of which was a function of a blind adherance to “pure” wool rather than blends. And the sheep population has declined radically, too, which probably has not helped the price of lamb at the supermarket.*

In fact, over time, it has been the common practice to turn over board membership each time the colour of the government changed (not noticeable recently as few state governments have changed in recent years). And when a code or the industry strikes problems the usual response is that the Minister plays musical chairs rather than reforms the system.

Yet it is that system which is the root cause of current difficulties. State authorities are responsible to no-one in practical terms. The stock market does not grade them and they do not have to satisfy the annual meeting of stockholders. They are typically charged with the “development and progress” of the industry yet no devices appear to exist to measure their success, or to generate action if no progress is made. Asset values have declined but are not reported widely if at all (and local or state governments play a role here as they own many racecourses). Survival seems to be a sufficient achievement.

Industry Culture

At the heart of the matter is the relationship between the industry’s culture and structure on the one hand, and its decision-making processes on the other.

Or, as Patrick Smith commented in The Australian (albeit on another aspect of the subject), “The ARB (Australian Racing Board) is compromised. Because it is not independent it is easily manipulated by an industry that is both driven and riven by self-interest.”

Actually, racing can be split into two parts: profit and non-profit. Raceclubs and state authorities are non-profit and their committee members are normally unpaid or lowly paid anyway. Yet participants, service providers and associated organisations such as TABs or bookmakers have to make a living like most of the population, or else they disappear.

However, as the Commission has already identified, the fortunes of clubs and authorities have been declining for many years now. That contrasts with …

> (a) the profitability of TABs, major training and breeding establishments (but not necessarily small ones), feed and medicine manufacturers and the like, and
> (b) major advances in technological fields such as communications, animal husbandry, drug testing, training methods, transport and so on, where Australia is often a world leader

The reasons for that differential have to be sheeted home to racing management. If finances are poor then clearly the use of the industry's assets, including human assets, must be suspect.

The broad reasons for that shortcoming are not hard to find. Basically, raceclubs and racing authorities have remained unchanged throughout all their existence. The names change occasionally but the structure never varies. Indeed, it is notable that state governments, which have the responsibility for setting up racing authorities, regularly play musical chairs without actually creating bodies which can better cope with a changing world.

Moreover, governments sometimes are inclined to take steps which downgrade the need for long term vision and development in order to satisfy short term political objectives. For example, the original sale of the government-owned TAB in NSW – by tender for an exclusive long term license – was designed to maximise the immediate capital return to government and not necessarily to create the best long term environment in which the industry might flourish. In Victoria, the racing industry was convinced to agree to TAB privatisation because the package included what could be called the unearned bonus of an ongoing share in state poker machine taxes (sadly, soon to disappear)

On top of that, ongoing regulatory changes were all designed to protect the newly privatised TABs and maximise their turnover. Little regard was paid to any effect on competition or industry financial development. Such measures included further restraints on day-to-day bookmaker operations as well as bans (albeit not very effective) on advertising and customers' use of interstate or overseas betting firms.

In other words, governments and racing authorities were unconcerned about generating competition, were not looking very far ahead, and ignored the winds of change.

As I mentioned in my original submission, specific warnings about those trends came from leading Sydney bookmaker Mark Read at an industry seminar in 1992. In effect, he advised authorities to shape up or he would have to withdraw. Read now runs IASBet in Darwin.

At that time, the "authority" was in fact the AJC, the Principal Club of the day, whose larger role has since been supplanted by Racing NSW (and similarly, too, in most other states).

The Commission must therefore note that inefficiencies were obvious prior to the formation of NT bookmakers as a group. Indeed, those same difficulties were the *reasons for their emergence in the first place. The failure of state authorities to better manage their business provided the foundation for the current regime.*

More worrying was that the racing establishment did not learn from its experience. Worse, it declared war on people who were their customers. Aggressive and even abusive (eg “parasites”) attitudes to NT bookmakers and betting exchanges continue to this day, especially in NSW, Queensland and W.A. Racing NSW media comments about the draft report of the Commission continue in that vein.

It is pointless to argue that Victoria, in contrast to some other states, has belatedly worked more cooperatively with NT bookmakers and Betfair when their home operations are messy, and there is constant bickering within clubs and between club groups.

Consider the views of Victoria’s top three bookmakers (Herald Sun, Feb 20, 2007). Paul Johnson said Winbet had worked seven days a week trying to build its internet business, but "ridiculous" rules and associated overheads had made it inoperable. Simon Beasley said another difficulty faced by bookmakers was that race club boards were run by "old-school mentality" with a “lack of understanding on the evolution of betting, punter habits and the introduction of betting exchanges”. Alan Eskander advised "We fall short in Victoria in two areas. First and most pronounced is that we can't bet on racing seven days a week from where we want to and we can't bet on whatever product we want."

Comparable comments have come from NT bookmakers previously based in Brisbane and Adelaide.

An oddly structured and motivated panel of state government bureaucrats (the 2003 Betting Exchange Task Force) also walked the same path when it found that the emergence of betting exchanges would cause untold damage to the industry. Its methodology was suspect and its findings simply echoed the emotional claims by the same governments and racing authorities which initiated their work.

Similarly, in another example, the report to the AJC by Access Economics on the alleged risks that would arise should betting exchanges prosper has dubious value – one never knows what the brief was.

The major state authorities’ attitudes to the intruders were frequently carried through to other codes and raceclubs, usually (again) without conducting proper evaluations or considering longer term implications and the wishes of their customers. For example, at the time the chairmen of both NSW and Queensland greyhound authorities were roundly abusive of both NT bookmakers and Betfair and warned participants to keep away from them as they were bad for the industry. Oddly, things have changed since and cash is now flowing through from the recalcitrant betting shops (amazingly, Betfair has just become a long term lead sponsor of NSW greyhound racing). But nobody has apologised for the abuse.

(A disclaimer: A few years ago, I was sacked as a columnist – a popular one, too - by two prominent greyhound publications for (a) pointing out that Betfair was here to

stay and the industry had better get used to it and (b) hinting that slow-acting committees of management were retarding the industry. So much for free speech).

The key point about all the above comments is that it tells us that the racing industry is blinkered, reactive and makes few if any rational decisions. A company making widgets, when faced with a declining customer base, will normally look into the matter and start making better or more appropriate widgets. Racing did not even consider this as an option. Forcefully, it told its customers they were wrong.

Why is this so?

While the Commission makes much of economic factors affecting some elements of betting over the years, it has not looked into the why and wherefore of the decisions the industry did not make or some choices they did make.

The raceclub, which is the beating heart of the industry, and its board or committee is representative of no-one except a handful of members (perhaps more than a handful in the case of a few large raceclubs). The structure tends to be autocratic as strong personalities dominate proceedings. Even then decisions by committees tend to create a camel when they were looking for a horse. At best, a lower common denominator syndrome applies.

In any event, raceclubs are frequently subject to internal dissention as one faction fights another or even (in an Adelaide case) experience outright illegalities in election processes. The Minister’s consultant in SA found that the SA harness organisation was subject to hopeless conflicts of interest which were damaging the sport.

Either way, faithful committee members and working bees historically ensured the survival of the club – seldom prospering, more often just staggering through – and were proud of the fruits of their labour. Outside advice and technological gains were not wanted to help build, maintain or improve the castle.

For decades, the industry got away with this process as customers lived around the corner and decisions produced quick reactions, for and against. That stopped happening 20 years or more ago with the arrival of SKY and the enrolment of distant customers with neither the means nor the desire to interact with the raceclub. The product was all they were after. Yet raceclubs kept ploughing on the same old way. Not only were their customers relatively disinterested in the club but the club was disinterested in them.

In turn, history tells us that leaders in those same raceclubs comprised or heavily influenced membership of state authorities – sometimes on an ex officio basis. Hence the level of conservatism transferred with them

Any attempts to create a degree of independence in state authority membership have been barely fruitful as almost always a previous affiliation must colour the attitude, or actually constitute a direct conflict of interest. There are exceptions – the SA greyhound authority is one – but by and large authority members arrive with a specific association with some aspect of the industry. In part, that’s not necessarily a bad thing, so long as it is balanced by independent thought, especially from the leadership of the group. But how often does that happen? And even when it does an historical industry or code culture tends to influence proceedings.

It's the system that's broken.

On the Quantity of Racing

This will be a never-ending argument but it won't be a productive one.

Yes, there are piles of rubbish races around which serve only two masters – the TABs that want all-hours coverage to keep money turning over, and the racing public in far flung areas.

The TABs also cover numerous international races where customers would not have the faintest idea of the quality of the runners or the nature of the tracks. Once again, they are seeking to exploit mug gamblers.

Having said that, they generate some cash that would not otherwise be available. It happens directly via normal TAB investments on local races and indirectly via regional publics becoming racing fans and supporting the TAB calendar or the industry at large.

Cut them out and total turnover will drop and some assets will be less efficiently utilised. It may be difficult to reduce costs proportionately.

The trick is to first make sure that the rubbish does not interfere with quality racing. Low quality races should never attract runners that can handle better stuff – ie management should tighten up on runners going into TAB races while supporting a reasonable quantity of provincial and country racing – as nurseries, in effect - that is not covered by the TAB.

However, more concentration on punter education and better publicity of quality runners can generate greater punting interest. Two things can help. First, bigger prize money differentials between high quality and low quality races. Here, I am not talking about multi-million dollar events (which, arguably, are already over-funded) but about week to week hardcore racing. And some tightening up of TAB programs (eg eliminating maidens) could allow the marketing machine to push races which generate greater public interest.

On Authority and Control

On p13.33 the Commission states that the three national racing bodies - Australian Racing Board, Harness Racing Australia and Greyhounds Australia (sic) – "represent state and territory racing authorities" and "have the competency and infrastructure required to run national levy scheme".

The Commission's appreciation of the industry may be stretched here. Those bodies are basically chat groups which may have agreed to set or accept certain national standards – on the rules of racing, for example – but where most commercial or other matters are taken under advisement subject to later consideration by individual state authorities or state governments.

The national body as such has no special or specific authority to act except as members have agreed to do so on a case by case basis. In practice, a supposedly general view is often in conflict with one or more state views, as is the case with gross revenue v turnover-based fees.

** The greyhound organisation is actually Greyhounds Australasia Ltd. New Zealand is an active player.*

Direct Distribution

The Commission itself has really torpedoed the possibility of directly distributing betting commissions to the clubs involved, but it does ask for comments.

The theory is fine in that better performing raceclubs should reap the rewards of their endeavours. However, since the opportunity to cash in on more lucrative slots is controlled by the state authority the question becomes academic.

Times of the week are massively influential in turnover levels, particularly where turnover comes from mug gamblers. In turn, customers' social and work habits dominate those preferences.

The current practice of the state authority assigning times and dates should continue. However, there is some evidence that inertia, politics and "possession being nine points of the law" have kept authorities from making tough decisions – ie about poor performing clubs. Here is yet another reason for less politics and more independent, business-oriented management within those authorities. Were that available, each code could no doubt organise incentives and rewards for good performers.

A Note on Racing NSW

RN claims that the lopsided distribution of NSW TAB commissions – where greyhounds subsidise the other two codes – is matched by the gallopers kindly allowing greyhounds to maintain their exclusivity on Saturday nights. To use RN's own language, this is rubbish.

First, it is not an exclusive slot as harness racing massively dominates Saturday nights, and always has.

Second, night racing is not popular with thoroughbred participants and is generally not successful anyway. Moonee Valley apparently manages reasonably on Friday nights but otherwise the practice is a disaster, especially in Sydney where attendances vary between dismal and hopeless.

The RN claim is specious and mischievous.

The End Solution

Racing desperately needs major reform and an injection of commercial discipline, together with improved governance and greater accountability – at raceclub, state and national level.

Independent national bodies, with teeth, are essential in each code to ensure imaginative and productive long term decision-making.

But it's governments that set the rules. They must now take note that their traditional ultra-conservative practices have been overtaken by national and world events and urgently need major reform.

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