

Maryland Tax Education Foundation
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MEDIA RELEASE

**MTEF Study Shows Majority of Maryland Racing
Purses Go to Out of State Owners**

**How Will Using Slots Money to Increase Purses
Benefit the MD Horse Industry?**

- 58% of thoroughbred racing purses went to out of state owners in 2007. Only 42% went to MD owners
- Of the 42% going to MD owners, the top 100 recipients garnered three fifths of this amount. This indicates a small group of MD owners will reap most of the local financial benefits from higher purses.
- The proposed 15,000 slot machines for Maryland should generate \$100 million per year in higher purses. Based on 2007 results, most of that money will go out of state. Raising purses seems to be an inefficient way of stimulating the MD horseracing industry, or of increasing green space.

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Higher Purses and Maryland Racing

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ABSTRACT

This short paper reviews the distribution of Maryland thoroughbred racing purses for 2007. It shows the majority of purses go to out of state owners.

The upcoming Maryland referendum on slot machines allocates up to \$100 million per year to higher purses. The rationale is based upon the often stated, but unproven, premise that higher purses stimulate racing and breeding activity, and increase Maryland greenspace.

The referendum has few provisions that will reverse the out of state dynamic, so a large portion of the purse subsidy will go out of state.

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Background

The horse industry in Maryland has a quality tradition, culminating each year in the Preakness stakes, one of the jewels in horse racing's Triple Crown. The industry operates two major thoroughbred tracks and, on a limited basis, two smaller harness tracks. One harness track suspended live racing operations until November 2008. Abbreviated meets are held at Timonium Fairgrounds and Fair Hill. The owners of Delaware Park have a license to conduct a short meet at a new thoroughbred track approved for Western Maryland.

Despite having legal monopolies, horse tracks nationally have struggled in recent years to provide satisfactory returns on investment. The reasons for this situation include: (i) a secular decline in interest in horseracing; (ii) the failure of the industry to keep up with changes in the sports, gaming and entertainment market; (iii) the inability or unwillingness to invest in new facilities; (iv) the lackluster returns on major investments that were made, such as Magna Entertainment's commitments to Gulfstream and Laurel Park; (v) changing management teams; (vi) an emphasis on slots as opposed to racing; and (vi) Internet, phone and cable TV betting that pays the tracks less than live wagers.

Like the major stockholders of Maryland football and baseball teams, the local industry stakeholders (tracks, breeders and horse owners) have sought subsidies from the taxpayers. In November 2008, Marylanders will vote on a referendum that would permit the operation of five slots-gaming facilities in the state, with a combined total of 15,000 machines. To reduce the windfall profits accruing to casino license holders, the state would impose the highest gaming tax in the nation, and some of the resulting revenue would subsidize the state's horseracing industry by supplementing race purses and capital investments. It has provided for a license awarding procedure that has the potential for competitive bidding for several of the licenses if the referendum is approved.

The annual slots win is estimated at \$1.5 billion, using win statistics from similar areas. Up to \$140 million per year of potential tax revenue from the machines will be diverted from the state treasury to the industry's stakeholders. Over the first eight years of the arrangement, the state could forfeit \$1.1 billion in tax revenue.

In part, referendum supporters argue that the huge subsidy is justified because; (a) higher purses boost racing activity; (b) only slots, as opposed to other financial aid, can bail out the industry; (c) without slots, the tracks will close, breeding will collapse and thousands of jobs will be lost; (d) if breeding declines, horse farms will be "paved over" by developers; and (e) the loss of an estimated \$600 million in state taxes from slots will endanger education funding, teacher salaries and teacher pensions.

Supporting several of these justifications are racing myths, none of which have been demonstrated by the industry, nor critically examined by the state government. By shedding light on actual conditions, this report should prove useful to voters and state decision makers.

Existing Distribution of Purses

MTEF determined the following distribution of thoroughbred purses in 2007 (in millions):

Out-of-state owners	58%	\$ 24.2
In-state owners	<u>42</u>	<u>17.4</u>
Total	100 %	\$41.6

Of the \$17.4 million received by in-state owners, the top 100 recipients garnered \$10.1 million. This is 58% of the MD amount ($10.1/17.4= 58\%$) and 24% of the total purses ($10.1/41.6=24\%$).

The data shows that 82% of thoroughbred purses are concentrated among out-of-state owners and a small group of Maryland owners (58% out of state + 24% top 100 MD = 82%). The study did not examine standardbred purses, which are far less than thoroughbred purses.

Distribution of Future Purses With Slots

Based on slots revenue projections that are consistent with other states, a reasonable estimate of future purse subsidies is \$100 million per year. Absent changes in distribution, the state is on target to send \$58 million (or 58%) of this potential tax revenue to out-of-state horse owners each year. \$24 million or 24% will go to the top 100 MD owners/recipients (an average of \$240,000 per year per owner).

Problems With the Industry's Justifications for Slots

The horse racing industry offers a number of justifications for why the state should subsidize the industry with slots. Many of the justifications do not withstand scrutiny:

Higher Purses Boost Racing Activity: A number of states divert a portion of slots revenue to increase purses. This classic argument supporting this policy is: "Higher purses attract better horses to the racetrack. This makes racing more interesting and encourages more bettors (live, in state OTB and out of state simulcast) to bet on the races."

However, this argument has shown to be a false promise. Research conducted by MTEF, the *Baltimore Sun* and others show no significant increase in handle, racing days or breeding in most states that subsidize purses. What increases there are seem to be driven by the fact that a new track owner must offer racing in order to obtain a slots license. Such licenses typically have been awarded by states governments for free or at a bargain price.

Delaware has more than doubled its tracks' purses, using subsidies from slots gaming. Yet, field sizes are smaller than Maryland, and Delaware lacks a breeding industry more than ten years after slots legalization.

In 2007, Pennsylvania practically tripled purses with slots revenue. However, total handle dropped by 4% versus 2006. The industry can argue that betting might have declined more without the higher purses, but how does the money support industry revitalization if it merely stems a decline? Racing days in Pennsylvania rose by 10%. Two new track openings accounted for the gain. Both openings were required for the owners to obtain lucrative slots licenses for a fraction of market value. From 2006 to 2007, the number of Pennsylvania foals fell from 1,255 to 1,207, according to the authoritative Jockey Club annual report.

Other Forms of Financial Aid: The state of Maryland provided substantial aid to baseball and football teams without slots. At the initial grant, both teams were controlled by out-of-state owners. The bulk of the subsidy went to in-state construction initially. Targeted horse racing subsidies might mean more tax revenues retained by the state.

Without Subsidies, Jobs Would Be Lost: At least two racetracks in the United States have closed in the last 10 years due to poor business conditions: Hialeah (Miami, Florida) and Great Lakes (Muskegon, Michigan). Bay Meadows (suburban San Francisco) is closing in late 2008 in order to be replaced by a large real estate development. Rosecroft's suspension of live racing reflects ongoing demand problems for harness racing, but the management has planned a November 2008 restart. Many U.S. track owners may not be realizing optimal profits in some cases, but returns seem sufficient to maintain operations.

In Maryland, slots supporters frequently attribute 30,000 jobs to the industry. Studies by the University of Maryland and MTEF put the number at 8,300 to 8,900. Each job is important, but taxpayers have to decide if the proposed subsidies are appropriate. Assume an extreme case, where 50% of jobs are lost without subsidies. The approval of the referendum saves 3,750 jobs. The annual purse and track renovation subsidy will be up to \$140 million, or \$37,000 per job per year.

No Slots Means Horse Farms Will Be Paved Over: Many horse farms are located in rural areas that do not lend themselves to intense commercial or residential development. If the goal of the referendum is to preserve open green spaces, the state could simply take the \$140 million per year and buy farmland or protective easements. Prices for farmland range from \$5,000 per acre in outlying counties to \$35,000 in closer-in counties (e.g., northern Baltimore County). At an average price of \$20,000 per acre, the state could acquire 7,000 acres of farmland per year, or 12 square miles. In seven years, the state could amass an area the size of Baltimore (80 square miles). By acquiring less-expensive easements in lieu of outright purchases, the state could multiply this total by several times.

Helping the Budget Crisis: Tax proceeds from slots could be maximized by: (i) a clear auction of slots licenses, rather than the process envisioned; (ii) legalization of casinos with table games rather than just slots; and (iii) locations that are more convenient to the population centers of MD, DC and Virginia. Indianapolis sold two slots licenses for \$500 million in April 2008 (the market value was appraised at \$700 million), and the state of Illinois is auctioning off, for the second time, the 10th casino license in that state. The referendum does address revenue maximization.

Maryland Slots Win Dedicated to Racing Subsidies

Seven percent of the slots win, not to exceed \$100 million annually, would be dedicated to higher purses. Eighty percent of this amount would be allocated to thoroughbred purses and 20% to standardbred purses. Fifteen percent of all purses would be targeted for Maryland-bred horses. In 2014, the State Racing Commission will study the impact of the higher purses on the industry and make recommendations concerning possible modifications. There is no provision in the enabling legislation for an independent study of such matters.

Another 2.5% of the annual win is dedicated to track renovations, with a maximum of \$40 million annually. The track owners must put up matching funds. This subsidy is eliminated after eight years. The maximum amount is therefore \$ 320 million (8 x \$40 = \$320). This amount is 60% of the cost of the new Washington Nationals baseball park.

Close to 80% of the \$320 million maximum is allocated to Pimlico and Laurel. Both tracks are owned by Magna Entertainment, a company that has attempted to promote and modernize the industry with varying degrees of success. The company is in financial distress, principally due to junk bond leverage, rather than failing racetrack operations. The state's investment is an outright grant, not a loan or equity security.

Fairness to Taxpayers and Consumers

The State of Maryland subsidizes (or protects from competition) a number of favored industries, from professional sports franchises to gas stations, funeral homes and health care providers.

Horse owners, breeders, and track owners are likely to be better off financially than the average Marylander. Are these fair subsidies? The industry might justify subsidy in light of concessions going to other sports, but is the \$140 million per year excessive? The targets of the subsidy, purses and renovations, have not turned the industry around in other states. Ideally, the state would like to see its funding directed to proven solutions.

About MTEF

MTEF is a nonprofit, non-partisan organization that studies budget and tax issues in the State of Maryland. Its most recent study covered private equity returns and the implications for public pension funds in Maryland. The website is:

www.marylandtaxeducation.org

About the Author

Jeff Hooke is the volunteer, unpaid Chairman of MTEF. He is the author of several books on finance and investment. He is a Baltimore native and resides in Chevy Chase, MD. A Managing Director of Hooke Associates, he was formerly an investment banker and private equity executive. He has written a number of studies on racing and slots. He has testified as an expert before several state legislatures on these topics.

Appendices

- A. Footnotes
- B. How the Study was Done
- C. Map of Owners Receiving MD Purses
- D. Table Showing Owners/Purse Recipients By State
- E. Top 100 MD Owners and Purse Recipients
- F. Jockey Club Statistics on Foals and Breeding by State

A. Footnotes

1. See MTEF's 2004 study, 'Horseracing and Casino-Style Gambling: Facts Behind the Myths.' *The Baltimore Sun* featured several articles in 2007 on slot machine revenues and their effect on tracks in nearby states.
2. See the Jockey Club's 2007 annual report and its foal statistics by state, which are summarized in Appendix F.
3. Pennsylvania Gaming Control Report dated July 24, 2008.
4. As the San Francisco newspapers have covered, the Bay Meadows real estate will be converted into 1,034 housing units and additional commercial buildings.
5. See MTEF 2004 study above. The University of Maryland study entitled, "Economic Impact of Horseracing in Maryland," was commissioned by the state legislature and completed in 1999.

MAPPING METHODOLOGY

Address lists of licensed Thoroughbred owners and trainers were provided by the racing commissions in Maryland and Pennsylvania. Address information was checked for quality control using a variety of mapping tools.

Steps taken to ensure the accuracy of addresses included:

- Corrected city, state, province (Canada) and zip codes where necessary
- Mapped addresses by street address and/or zip code
- Eliminated duplicates or dummy entries (e.g., "Test")
- Corrected anomalies in name spellings where identified

Racing information for races conducted at Laurel Park and Pimlico Race Course during 2007 was recorded from published race entry and results information, and included the names of racehorse owners, purses earned, foaling state of each racehorse, *etc.*

Next, owners' earnings were matched with license information. The list of licensed Maryland owners and trainers only included those licensed to race in 2008. Therefore, the Pennsylvania list of licensed owners and trainers was also used for matching purposes.

Maryland provided the name of the principal partner for each stable, whereas Pennsylvania provided a complete list of stable partners. Therefore, for stables licensed in both states, the Pennsylvania stable list was used to proportionately allocate earnings among all stable partners. In cases where individual owners and trainers were licensed in both states, the address provided by the Maryland Racing Commission was used as the default.

Summary

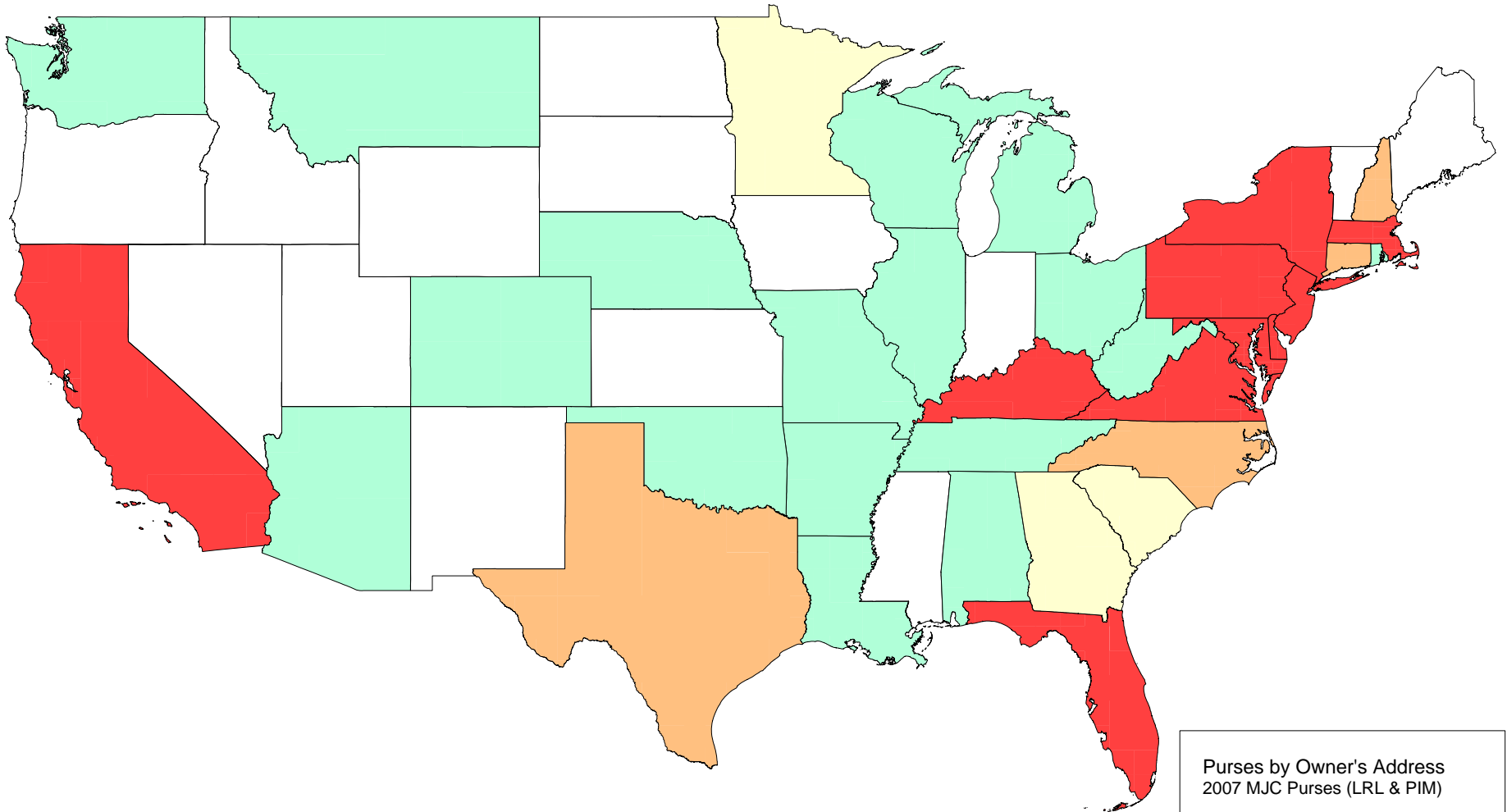
- All US and Canadian addresses provided by the racing commissions were mapped at least to the zip code level.
- 92.6% of purses paid were traced to some or all of the owners who earned them. We used the map coordinates of these owners to map their earnings. The Maryland list of licensed owners and trainers did not include those licensed in 2007 but not yet in 2008.
- Total thoroughbred purses were \$41.6 million at Pimlico and Laurel. 92.6% or \$38.5 million in 2007 were traced. MTEF did not manually trace the other 7.4%, or \$3.1 million, but a spot check showed most of the owners were out of state.
- 44.3% of traceable purses were for MD addresses, or about 41.0% of total purses (44.3% times 92.6% equals 41.0%).
- As an estimate, MTEF used 42%.
- Initial analysis of unmatched earnings (identifying the owners of the largest amounts and looking up their addresses from other sources) indicated that they were primarily from out-of-state – further analysis will be conducted once complete license information is available for 2007.

Caveats

- People with homes in multiple states list only one address on the license.
- Only US and Canadian owners and earnings were mapped.
- If several people owned a horse, but addresses weren't available for all of the individuals, the earnings were allocated to owners with addresses in our data.
- Some stables have many partners, each of whom might own only a portion of the stable's horses. We allocated the stable's earnings as if the partners were equal owners. It was an inexact science, but seemed better than assigning all of a stable's earnings to a single partner.
- Among Maryland-licensed owners and trainers identified by the Maryland Racing Commission as licensed in 2008 (as of May 15, 2008), 41.3% were from Maryland.
- If one were to further assume that MD owners and trainers win purses in the same proportion to out-of-state owners and trainers, then this 41.3% statistic corroborates MTEF's 42% estimate of purse earnings attributable to Maryland owners.

Note: The statistics were compiled by Charles Vickery, a nationally known racing consultant, under a contract with MTEF.

Purses Won at MJC in 2007 by State



Purses by Owner's Address
2007 MJC Purses (LRL & PIM)

■	500,000 to 17,100,000	(10)
■	250,000 to 500,000	(5)
■	100,000 to 250,000	(3)
■	1 to 100,000	(18)
□	0 to 1	(16)

ID	EARNED	Cumulative	Cumul.%
MDOT000424	623,460	623,460	3.66%
PAS00046401	604,638	1,228,098	7.20%
MDOT001826	412,120	1,640,218	9.62%
MDOT000159	380,820	2,021,038	11.85%
MDOT002404	279,840	2,300,878	13.49%
MDOT000340	210,020	2,510,898	14.73%
MDOT001604	183,570	2,694,468	15.80%
MDOT000025	172,440	2,866,908	16.81%
PAS00073301	172,440	3,039,348	17.83%
MDOT001396	172,289	3,211,637	18.84%
MDOT000308	167,392	3,379,029	19.82%
MDOT000682	159,430	3,538,459	20.75%
PAS00024901	153,331	3,691,790	21.65%
MDOT002507	151,958	3,843,748	22.54%
MDOT000795	147,655	3,991,403	23.41%
PAS00005401	123,590	4,114,993	24.13%
MDOT002311	121,540	4,236,533	24.85%
MDOT002226	121,064	4,357,597	25.56%
MDOT002112	120,770	4,478,367	26.27%
PAS00119701	120,770	4,599,137	26.97%
MDOT000126	110,320	4,709,457	27.62%
MDOT001574	105,860	4,815,317	28.24%
PAS00068601	105,316	4,920,633	28.86%
MDOT001275	104,015	5,024,648	29.47%
PAS00144101	104,015	5,128,663	30.08%
MDOT002114	98,760	5,227,423	30.66%
PAS00103001	97,175	5,324,598	31.23%
PAS00103002	97,175	5,421,773	31.80%
MDOT002496	96,420	5,518,193	32.36%
PAS00059901	93,900	5,612,093	32.91%
MDOT000324	89,492	5,701,585	33.44%
MDOT000519	88,920	5,790,505	33.96%
MDOT002259	88,227	5,878,732	34.48%
MDOT000899	88,075	5,966,807	34.99%
MDOT002303	87,080	6,053,887	35.51%
MDOT000312	85,510	6,139,397	36.01%
MDOT002015	85,380	6,224,777	36.51%
MDOT001231	84,900	6,309,677	37.01%
PAS00117101	84,235	6,393,912	37.50%
PAS00117102	84,235	6,478,147	37.99%
MDOT002124	81,550	6,559,697	38.47%
MDOT001752	80,893	6,640,590	38.95%
MDOT001627	80,580	6,721,170	39.42%
MDOT001543	78,830	6,800,000	39.88%
PAS00070701	78,696	6,878,696	40.34%
MDOT000623	77,240	6,955,936	40.80%
MDOT001426	77,240	7,033,176	41.25%
MDS000427	76,590	7,109,766	41.70%
MDS000444	75,860	7,185,626	42.14%
MDOT000348	75,550	7,261,176	42.59%
MDOT001545	75,540	7,336,716	43.03%

MDOT001969	74,707	7,411,423	43.47%
MDOT002162	72,700	7,484,123	43.89%
PAS00099901	72,402	7,556,525	44.32%
MDOT000494	72,380	7,628,905	44.74%
MDOT002482	71,088	7,699,993	45.16%
MDOT001855	70,460	7,770,453	45.57%
PAS00155301	68,670	7,839,123	45.98%
PAOT004378	67,680	7,906,803	46.37%
PAS00095501	66,430	7,973,233	46.76%
PAS00095502	66,430	8,039,663	47.15%
MDS000296	66,340	8,106,003	47.54%
MDOT000231	66,220	8,172,223	47.93%
MDOT001512	63,980	8,236,203	48.30%
MDOT001516	63,980	8,300,183	48.68%
MDOT000823	63,500	8,363,683	49.05%
MDOT000749	62,880	8,426,563	49.42%
MDOT001158	60,850	8,487,413	49.78%
PAS00038701	60,850	8,548,263	50.13%
PAS00119101	60,380	8,608,643	50.49%
MDOT001209	59,840	8,668,483	50.84%
MDOT000689	58,590	8,727,073	51.18%
MDOT000753	57,220	8,784,293	51.52%
MDOT000098	57,080	8,841,373	51.85%
PAS00139902	56,520	8,897,893	52.19%
PAS00131701	55,220	8,953,113	52.51%
MDOT000870	55,150	9,008,263	52.83%
PAOT005343	53,510	9,061,773	53.15%
MDS000260	53,390	9,115,163	53.46%
MDOT001503	52,860	9,168,023	53.77%
MDOT001223	52,444	9,220,467	54.08%
MDS000179	52,320	9,272,787	54.38%
PAS00158401	52,115	9,324,902	54.69%
MDS000528	51,660	9,376,562	54.99%
PAOT006545	51,050	9,427,612	55.29%
MDOT001034	50,820	9,478,432	55.59%
MDOT000736	50,810	9,529,242	55.89%
MDOT001301	50,210	9,579,452	56.18%
MDS000279	50,210	9,629,662	56.48%
MDOT000979	50,120	9,679,782	56.77%
MDOT001356	50,040	9,729,822	57.06%
MDS000294	50,040	9,779,862	57.36%
MDOT000954	49,880	9,829,742	57.65%
MDOT000846	49,639	9,879,381	57.94%
MDOT001233	49,639	9,929,020	58.23%
MDOT002448	49,600	9,978,620	58.52%
MDOT002179	49,415	10,028,035	58.81%
MDS000474	49,415	10,077,450	59.10%
MDOT001476	49,020	10,126,470	59.39%
MDOT001505	48,960	10,175,430	59.68%
PAOT002050	47,530	10,222,960	59.96%
PAS00017601	47,270	10,270,230	60.23%
MDOT000392	47,200	10,317,430	60.51%

FoalArea	Earnings	Starts	PctEarn	PctStarts
AL	370	1	0.00	0.01
AR	186,870	93	0.39	0.59
BC	3,880	7	0.01	0.04
BR	75,725	31	0.16	0.20
CA	405,305	172	0.85	1.09
CH	57,290	17	0.12	0.11
CO	220	1	0.00	0.01
FL	7,967,951	2,940	16.62	18.68
FR	8,230	6	0.02	0.04
GA	16,150	6	0.03	0.04
GB	31,100	18	0.06	0.11
IA	1,420	3	0.00	0.02
IL	77,600	19	0.16	0.12
IN	1,645	7	0.00	0.04
IR	66,385	20	0.14	0.13
JP	1,840	4	0.00	0.03
KY	13,577,433	3,963	28.32	25.18
LA	48,320	10	0.10	0.06
MA	26,450	26	0.06	0.17
MD	2,288,660	773	4.77	4.91
MI	18,850	11	0.04	0.07
NC	19,740	10	0.04	0.06
NJ	1,654,274	955	3.45	6.07
NM	19,770	6	0.04	0.04
NY	2,035,928	1,052	4.25	6.68
OH	53,120	21	0.11	0.13
OK	4,590	3	0.01	0.02
ON	475,455	189	0.99	1.20
PA	17,808,596	5,003	37.14	31.79
PE	40,430	9	0.08	0.06
PQ	3,045	2	0.01	0.01
SC	56,550	29	0.12	0.18
TN	160	1	0.00	0.01
TX	510,995	192	1.07	1.22
VA	336,701	115	0.70	0.73
WA	20,255	8	0.04	0.05
WV	43,000	15	0.09	0.10
PHA Totals	47,944,303	15,738	100	100

Lists Place Foaled and earnings for horses racing at PHA in 2007.
Data Source: Daily Racing Form Results Charts.
PHA: Philadelphia Park