

Submission by Tabcorp to the Director of Racing and Tasracing in connection with application under s 54C of the *Racing Regulation Act* 2004

1 Summary of what Tabcorp seeks

Tabcorp requests that the Director of Racing and Tasracing apply a turnover based race field information publication approval fee on an equitable and consistent basis to all wagering operators who are required to seek approval under the *Racing Regulation Act* 2004 (**RR Act**).

Tabcorp submits that revenue based race field fees should not be imposed, because revenue based fees:

- are not in the long term interests of ensuring a sustainable Tasmanian racing industry;
- are uncertain in their application and are capable of manipulation by wagering operators who seek to minimise their contributions; and
- do not result in wagering operators making a fair and equitable contribution to the costs of the industry upon which their businesses are based.

2 Introduction and background

2.1 Basis for this submission

This submission is made by Tabcorp Holdings Limited (**Tabcorp**) on behalf of itself and TAB Limited (**TAB**) as part of their respective applications for approval under section 54C of the RR Act for the period from 1 July 2009, and should be read in conjunction with the application forms submitted by Tabcorp and TAB.

This submission is intended to be considered by the Director of Racing and by Tasracing Pty Limited (**Tasracing**), in the latter's capacity as the representative body of the Tasmanian racing industry which is responsible for determining a fee for a race field information publication approval for each code of racing (under s 11(1)(qa) of the RR Act).

2.2 Commercial-in-confidence

This submission contains information which is commercially sensitive and confidential to the Tabcorp group. Its contents are intended only for consideration by the Director of Racing and by Tasracing in their capacity as the persons responsible under the RR Act for granting race field information publication approvals and determining the fees that will attach to such approvals. It is not for public release or disclosure to any other person or entity.

2.3 Tabcorp's business

Tabcorp and TAB have established outlets and totalisator agencies at locations throughout Victoria and NSW, and maintain telephone call centres and internet websites at which wagers may be made in relation to races and sporting events conducted in NSW, Victoria and in other jurisdictions, including Tasmania.

The principal business of Tabcorp and TAB is totalisator betting (although both have fixed odds businesses as well). TAB is the holder of the exclusive licence to conduct the off-course totalisator in NSW. TAB is a wholly owned subsidiary of Tabcorp, which in turn is the operator of the licensed totalisator in Victoria.

Both Tabcorp and TAB carry on significant totalisator business in relation to racing events throughout Australia, including in relation to Tasmanian racing events.

2.4 The wagering landscape

Totalisator betting has been the principal form of wagering in Australia. As you are aware, totalisator betting is a pari-mutuel system of betting in which the operator pools all wagers (turnover) and then deducts a commission. The remainder of the pool is distributed to punters as dividends in accordance with the outcome of the bets or contingencies. There are statutory limits on the amounts that can be deducted as commission from the pool.

As referred to above, TAB is the licensed totalisator in NSW and its parent company, Tabcorp, holds the totalisator licence in Victoria. Other totalisators in the Australian marketplace are:

- ACTTAB (which operates the totalisator in the ACT);
- UNITAB (which operates the totalisator in Queensland, South Australia and the Northern Territory);
- TOTE Tasmania (which operates the totalisator in Tasmania); and
- RWWA (which operates the totalisator in Western Australia).

Another form of wagering available in Australia is fixed odds betting, which is offered by licensed bookmakers as well as by TAB and Tabcorp. In recent years, an increasing number of corporate bookmakers, many based in the Northern Territory, have entered the market offering wagering services over the telephone and internet.

A third form of wagering offered in Australia in recent times is through use of a betting exchange. The only current licensed betting exchange operator in Australia is Betfair, which is of course located in Tasmania. Under the betting exchange model, prospective punters place bets that a particular outcome or contingency will or will not occur. The role of the betting exchange in the transaction is to:

- make information available by internet or telephone to prospective punters about each race, event or contingency occurring within Australia on which registered players may place a wager;
- 'match' opposing bets placed by registered players against each other; and
- deduct a commission on a basis and at a level determined by the betting exchange in question. Betfair, for example, has elected to deduct a commission from each registered player's net winnings. Betfair has stated publicly that its commission is typically in the range of 2-5%.

3 The significance of the Victorian Supreme Court decision

With the introduction of race fields legislation in various Australian jurisdictions in recent times, each of the racing controlling bodies in New South Wales, Queensland, Victoria and South Australia have made decisions stipulating the basis on which wagering operators will be charged fees for race fields. Similar decisions are expected to be made in future in Western Australia and the ACT.

As you are aware, TAB successfully challenged the race fields fee decisions made by Racing Victoria Limited (**RVL**) and Greyhound Racing Victoria (**GRV**) in respect of the 2008 – 2009 approval period. The decisions of RVL and GRV required TAB to pay product fees based on revenue, rather than turnover.

Tabcorp notes the decision communicated by the letter dated 21 September 2009 from the Director of Racing to delay the implementation of the condition for the payment of a fee for the publication of Tasmanian race field information.

The fee that was proposed to be introduced was “a fee of 10% of gross revenue”. Such a fee would have been substantially similar to the kind of fee introduced by RVL and GRV.

Tabcorp considers that Tasracing should now reconsider its decision to impose a fee of “10% of gross revenue”.

Tabcorp expects that the Tasmanian racing industry is currently focussing on the impact of that part of the decision in *TAB Limited v Racing Victoria Limited; TAB Limited v Greyhound Racing Victoria* [2009] VSC 338 which concerned the requirement imposed by the relevant provisions of the *Gambling Regulation Act 2003* (Vic) that any fee imposed must be of a stated amount, rather than expressed as a formula. As you know, this finding was based on the particular terms of the Victorian statute.

However, it is important to appreciate that the decisions made by RVL and GRV were set aside on multiple grounds. Most importantly for present purposes, her Honour Justice Davies held that a fee expressed as a percentage of gross revenue was uncertain in its application to wagering operators. The Court’s finding in this regard was based on common law principles that would also apply with equal force in Tasmania.

There are a number of fundamentally different ways that Tabcorp and TAB can calculate “gross margin”, and there are many complicating factors which make every such calculation uncertain. Her Honour describes out some of these factors in the judgment. While some of these factors are peculiar to totalisator operators, others will affect all types of wagering operators.

Her Honour also stated:

“It is clear from the evidence that TAB’s revenue from its operations is derived from several sources and the determination of the fee payable will involve a number of integers. It is readily apparent that the application of some integers will involve matters of judgment, about which there may be legitimate differences of opinion between TAB and RVL.” (paragraph 35)

Her Honour referred, by way of example, to the difficulties posed by needing to account for unclaimed dividends, bad debts, errors and customer claims, cross code/state/sports bets, timing issues multi-leg bets and free bets, before stating that:

“These are not issues of construction and interpretation. ... It is not an answer that actual uncertainty ought to be capable of resolution between the parties or, failing resolution, adjudicated upon by a Court applying ordinary principles of construction and interpretation, as submitted by senior counsel for RVL. In my view, RVL has failed to express its fee condition in terms that fix a definite standard or criterion by which the amount of the fee can be ascertained with certainty and the failure goes to the exercise of power and, in my view, vitiates the exercise” (see paragraphs 36-37).

Given these findings, in Tabcorp's view the concepts of "gross revenue" or "gross margin" have been comprehensively discredited. While some racing controlling bodies may seek to avoid these difficulties by providing ever more complex definitions and guidance, in Tabcorp's view this is more likely to promote uncertainty and disputation than be productive of its resolution.

This is because the wagering industry is extremely competitive, and the range of products and services being offered is becoming more complex and sophisticated. Each new type of product is likely to throw up unanticipated challenges for the calculation of revenue or margin. Obviously, this degree of complexity will increase the scope for unscrupulous operators to attempt to understate the amount payable, or even simple inadvertent miscalculation of the amount payable, which is likely to increase the auditing and compliance burden faced by the Tasmanian racing industry.

4 Why is the turnover model for all applicants the correct approach?

As the Minister for Police and Emergency Management noted in his second reading speech for the race fields legislation on 28 May 2009, the power to levy a race fields fee was designed as part of a series of measures designed to safeguard the sustainability of the Tasmanian racing industry over the longer term.

In Tabcorp's view, the ability to ensure a sustainable industry over the longer term will be best promoted by adopting a fee structure that requires all wagering operators who gain a commercial benefit from using Tasmanian racing product to pay a fee that is **directly related to the amount of wagering custom** generated by the wagering operator's use of the product, which is calculated on the same basis for all operators.

For the reasons outlined below, the turnover model of fee is the best and fairest way to achieve this over-arching objective.

Turnover is the best available measure of level of use of race fields

Under the proposed Tasmanian race fields information publication approval scheme, the payment of the stipulated fee is a condition of approval for any applicable wagering operator to publish Tasmanian race field information. There is an obvious and direct relationship between the approval, on the one hand, and the fee which the Director of Racing is authorised to charge for that approval, on the other hand.

Wagering operators (whether they be totalisators, bookmakers or betting exchanges) use and publish race fields as an integral and essential part of their ability to offer wagering services to prospective punters. This includes providing information to punters concerning the racing events and entrants in those events on which wagers may be placed. That use results in custom for the wagering operator. The total custom – in other words, the total amount of wagers which are placed by punters with a wagering operator is the fairest and best available measure of the level of use of race fields information made by that operator.

Turnover reflects volume of business and is a good measure of commercial success

The level of wagers placed with a wagering operator describes the volume of business that the operator is conducting. Not only does a greater volume of business indicate that the wagering operator is using and publishing race fields more, it is also the best measure of the operator's commercial success in attracting custom.

A primary objective of the race fields legislation is to ensure that wagering operators do not 'free ride' on the racing industry on which their businesses are based. That objective is best achieved by directly tying the race fields fee itself to the most obvious (and most difficult to manipulate) measure of the success of a business, being its turnover.

A turnover-based fee does not distort the market for wagering services

Wagering is the main source of funding for the Tasmanian racing industry.

The principal effect of a revenue based fee is that higher margin operators, such as the state based totalisator operators, will pay much larger amounts than lower margin operators, and will effectively subsidise the cost of Tasmanian racing product for lower margin operators.

This is not a fair or even handed regulatory response, because what appear to be higher margins for state based totalisators often do not take into account the very significant contributions to government revenue and industry funding that each of those operators make from those higher margins. To date, the result of encouraging the cross-subsidisation of lower margin operators by higher margin operators has been real reductions in the overall amount returned to local racing industries, because most of that funding is provided by the totalisator operators.

Turnover is common to all wagering operators, irrespective of business model adopted

All wagering operators have one thing in common. Their businesses are based upon accepting wagers placed by customers. Turnover, being the total amount of wagers, is the common starting point for all applicants for approval to use and publish race fields.

In contrast, revenue based fees are exposed to individual wagering operators' strategic and commercial decisions. A wagering operator may make many commercial decisions in the course of its day-to-day business which impact on its revenue or margin for any given period. A decision to charge a particular commission, to offer particular odds or to take a particular wager may result in vastly different revenue to the wagering operator for the period. For example, a corporate bookmaker may conduct a large volume of business during a particular month, but because of a single large wager offered at unusually long odds and not bet back, the bookmaker may suffer a loss for the month in question. A turnover based fee would insulate the Tasmanian racing industry from the vagaries of such commercial decisions.

Further, business models are not set in stone, but are open to manipulation or change by wagering operators. Turnover cannot be manipulated. However, gross margin or revenue may be, particularly because of the differing definitions of 'gross margin' or 'gross revenue' used in differing jurisdictions.

Turnover is a commonly adopted measure of fees or taxes in other contexts

The level of use of a product for which a fee is charged is a common basis for the calculation of the fee itself. For example, an analogous situation is the royalty or fee charged for the use of copyright works in the context of intellectual property. In such cases, a common method for calculating the fee is according to the level of use of the work in question, particularly where multiple non-exclusive licences are granted.

Wagering operators are familiar with assessing turnover as a basis for calculating fees and taxes they are already liable to pay. For example, NSW bookmakers pay fees to NSW racing clubs based on turnover. Australian wagering operators who place bets in some international jurisdictions (such as New Zealand, Hong Kong and the US) are charged turnover based fees for doing so. The NSW thoroughbred and harness racing bodies, the Victorian harness racing body and all of the Queensland racing codes levy race field fees based on turnover. Greyhound Racing Victoria has recently stated that it is proposing to move to a turnover based fee following the decision of the Supreme Court of Victoria described above.

Turnover is simple for wagering operators to calculate and for regulators to administer

Many wagering operators would already be calculating turnover for the purpose of other fees or taxes (as described above). For those operators who do not already pay any turnover-based taxes, turnover is a fundamental aspect of their business and it is reasonable to assume that it is data which all wagering operators gather for internal

purposes. The total amount of wagers placed with any particular wagering operator is not susceptible to arguments as to what should be included or excluded. It does not require the exercise of any discretion, judgment or opinion.

A fee for race fields information based on turnover is not likely to place any significant additional administrative burden on a wagering operator in terms of data collection. This differs from any other basis for collection of the fee, such as any definition of 'gross revenue' or 'gross margin', which may be a concept which has no application outside the realm of the particular race fields fee in question.

Just as turnover is a simpler and more uniformly understood concept than the many differing definitions of gross margin or gross revenue, turnover is also a straightforward measure for the Director of Racing and Tasracing to assess and administer. This is particularly important where the relevant wagering operators are located outside Tasmania. The Director of Racing and Tasracing have limited capacity to audit the operations of interstate operators (for example to ensure that wagering operators do not place sham bets after the running of a race in order to reduce their declarable gross profits, or carry out other avoidance techniques).

A revenue-based fee will always cause uncertainty and confusion in its calculation

Tabcorp and TAB experience great difficulties calculating with certainty the amount of fees imposed under revenue or gross margin based fee regimes. As the Supreme Court of Victoria has held, the difficulties are real. They are multiplied in the case of contingencies which include different codes or events (such as multiple contingency products like "The Big Six", or events that are jackpotted), because of the complex and conflicting rules for apportionment of gross profit that are being put forward, without any attempt at coordination, by the regulators for different codes in different jurisdictions.

Tabcorp considers that even if the Director of Racing considers each specific issue relating to a fee based on gross margin as the issue arises and attempts to give guidance to operators, there are likely to be ongoing disputes about the interpretation and proper application of such a formula, and considerable scope for operators to adopt measures to avoid or minimise the amount of fees they are required to pay, such as by manipulating the use of bet backs and by using book management arrangements between related entities.

Of course, in this regard, while some operators - like Tabcorp – may elect to bring those matters to the attention of the Director of Racing in an attempt to obtain clarification, other operators may choose not to do so, and they will only become apparent if Tasracing is prepared to carry out detailed and costly audits of operators' financial records.

As things stand, each of RVL, Greyhound Racing NSW, and Racing SA has sought to impose revenue or gross profit based race fields fees upon Tabcorp and TAB. Each has adopted a different approach to the calculation of the fee sought to be imposed. For example, Tabcorp and TAB face the possibility of having to collect and collate data to meet the following differing definitions raised in the context of race fields to date:

- '10% of revenue derived from betting on Victorian thoroughbred race fields (exclusive of GST);
- '10% of the Approval Holder's Gross Margin where Gross Margin is the amount calculated as follows in connection with a NSW Greyhound Race (or contingency relating to a NSW Greyhound Race) conducted during the Approval Period: NSW Greyhound Turnover less punter winnings less Eligible Bet Backs plus Eligible Bet Back Returns.
- 10% of Monthly Gross Proceeds, where Monthly Gross Proceeds means the aggregate of ... any and all bets or wagers taken or received by the Operator on or in respect of a South Australian Race, less any dividends paid out by the Operator to the Customer in respect of those bets or wagers (all excluding GST) ... adjusted for any Authorised Bet-Back made by an Operator.

Most of these formulas contain a number of defined terms within the main definition, and many of those defined terms are in turn made up of further defined terms. If each regulator for each different racing code in each State or Territory imposes a revenue based fee with different rules and different exclusions, the administrative burden upon Tabcorp and TAB of complying with the various schemes will soon become oppressive. Tabcorp and TAB will be exposed to very significant additional costs, which in turn will diminish the returns they are able to make to the racing industry as a whole. Further Tabcorp and TAB's systems do not accommodate such complexities and they would face significant management and systems costs in converting their systems. Again this would diminish returns to the racing industry as a whole. This would be a remarkable outcome in circumstances where governments throughout Australia are currently cooperating to reduce the compliance burden faced by businesses of all kinds.

Given that the Director of Racing and Tasracing are responsible for administering the race fields scheme in a manner which is most likely to promote a sustainable Tasmanian racing industry, Tabcorp considers that the fee structure Tasracing decides to impose should be transparent, capable of straightforward application by operators and lend itself to easy verification of operators' compliance.

For the reasons set out above, a fee based on wagering turnover meets these criteria. Tasracing should not adopt a fee basis which is likely to lead to a large number of rules and issues which need to be applied specifically to particular operators, and thereby create a potentially very large compliance burden for both itself and for wagering operators.

A turnover-based fee provides the Tasmanian racing industry with greater certainty

A revenue based fee leaves the Tasmanian racing industry exposed to the movement of wagering custom from high margin operators to low margin operators.

Where a race fields fee is levied on all operators according to turnover, then the industry's income stream is not exposed to the risk of punters switching business from a high margin operator to a low margin operator.

Allegations that a turnover-based fee unreasonably impacts on the viability of individual applicants are unsubstantiated

Betfair has claimed in its legal proceedings challenging the NSW thoroughbred and harness race fields fee regimes that a fee based on turnover threatens its ability to compete. Betfair may well make similar assertions to the Tasmanian racing industry in order to demand the imposition of a fee levied on a basis other than turnover.

There are a number of reasons why such unsubstantiated threats should be scrutinised carefully:

- Betfair has determined to adopt a business model which relies on charging a commission in the range of 2-5% of a registered player's net winnings only. This is a self imposed restriction. Betfair's calculation of how a turnover-based fee translates to a revenue-based equivalent is silent on the question of whether it would be able to increase its commission, to impose a commission on all customers, rather than winners only, or otherwise to change its charging structure in order to increase its revenue to meet its overall outgoings, including race fields fees.
- Alternatively, a wagering operator should be able to pass on any turnover-based fee in full or in part to customers. Given the direct correlation between the value of bets placed and the turnover-based fee, it would be simple for a wagering operator to pass part or all of the fee on to consumers. Taking the example of a fee set at 1.5% of turnover (a percentage that has been adopted by Harness Racing Victoria, Racing New South Wales, Harness Racing New South Wales and the 3 racing controlling bodies in Queensland), even if the entire fee of 1.5% were passed on, the incremental increased cost to the end-user is small. Betfair's claims have not been substantiated in any way, and as

far as Tabcorp is aware Betfair continues to offer wagering on the racing products of those codes.

- The High Court judgment in *Betfair v Western Australia* [2008] HCA 11 at [107] provides as follows:

*“The evidence shows that by agreement with the Victorian regulator, Betfair undertook to return **an amount equivalent to one per cent of the value of bets taken by it on races in Victoria**; this is the same level of return as that required from bookmakers in that State. Betfair has been meeting that obligation. There is no reason to doubt the assertion by Betfair that it remains ready to undertake obligations of this kind in Western Australia and to ensure that the organisers of races in that State obtain a reward from Betfair as well as from other wagering operators in that State.”*

[emphasis added]

If this is an accurate summary of a submission made on behalf of Betfair to the High Court, Betfair has accepted that it would be willing and able to remit a fee based on 1% of turnover to Victorian regulators. No question of the impact on the viability of Betfair's business appears to have been raised in that forum.

- In addition, Regulation 5A of the Gaming Control Regulations 2004 (Tas) has the effect of alleviating the impact of race fields fees in other jurisdictions on Betfair. In these circumstances Betfair cannot maintain an argument that a turnover fee impacts on its ability to compete.

Further, in relation to corporate bookmakers, we understand that the Northern Territory government is amending its legislation so as to adjust betting tax to compensate for the fact that corporate bookmakers have to pay race fields fees in other jurisdictions. Thus Northern Territory based corporate bookmakers will not even pay tax in their home jurisdiction. In those circumstances it is difficult to see how any allegation of unreasonable impact on viability can be maintained by the Northern Territory based corporate bookmakers.

Any fears that a turnover-based fee would discriminate against interstate operators are unfounded

In Tabcorp's view, there are no constitutional issues which are likely to arise from any decision made by Tasracing to impose a uniform fee on a turnover basis, given that any such fee would be levied in a uniform way on all operators, including the intrastate totalisator, the locally based betting exchange and interstate wagering operators.

A fee based on gross margin or revenue does not have a direct correlation with capacity to pay

It has been said that a turnover-based fee has no necessary correlation with the capacity of a wagering operator to pay the fee. However, the same criticism can be levelled against a fee based on gross margin or gross revenue.

The concepts of 'gross margin' and 'gross revenue' are blunt instruments. They do not take into account the vast differences in fixed expenses and liabilities of the differing wagering operators. A uniform fee based on a percentage of gross revenue has a vastly differential impact on wagering operators because it does not compare like with like.

Wagering operators with very low cost base operations have a much greater portion of their 'gross margin' or 'gross revenue' available for their disposal to meet a fee such as the race fields fee. Wagering operators like totalisators, in contrast, have very high existing liabilities which must be met out of gross margin/revenue before any new fees or expenses can be paid. In the case of Tabcorp and TAB, these significant existing liabilities include:

- betting tax in NSW and Victoria;
- economic contributions to the local State racing industry;

- existing contributions to the racing industry over and above the product fees (such as sponsorships, interest free loans and donations);
- payments to data providers;
- commissions for Tabcorp and TAB agents, and outlets in pubs and clubs;
- third party providers of wagering service providers such as FOXTEL, TwoWayTV and any future licensed secondary operators of Tabcorp's online betting websites;
- pooling fees paid to other wagering operators;
- bad debts, shortfalls in agent or outlet receipts;
- premium customer rebates; and
- maintaining, servicing and updating the Tabcorp group's extensive retail infrastructure in addition to its telephone and internet presence.

For that reason, the argument that a fee based on turnover does not take into account a wagering operator's capacity to pay is just as applicable to a fee based on gross margin or revenue.

5 Other matters

Tabcorp does not believe that there is any other reason why a uniformly applied fee based on turnover would be invalid and liable to successful legal challenge. However, if the Director of Racing or Tasracing considers there may be some other basis, Tabcorp would seek the opportunity to be informed about those matters and be given an opportunity to consider and make appropriate submissions about them.