

GOVERNMENT LAW CENTER OF ALBANY LAW SCHOOL
GOVERNMENT LAW ONLINE

WHAT DO WE DO ABOUT REBATES?

NOVEMBER 2003



80 New Scotland Avenue
Albany, NY 12208
www.als.edu

GOVERNMENT LAW ONLINE publications are available at www.governmentlaw.org

WHAT DO WE DO ABOUT REBATES?

**Bennett Liebman, Esq.
Coordinator/Staff Attorney
Racing and Gaming Law Program**

NOVEMBER 2003

These materials are copyright by Albany Law School (ALS) on behalf of its Government Law Center or ALS licensors and may not be reproduced in whole or in part in or on any media or used for any purpose without the express, prior written permission of Albany Law School or the licensor. Neither Albany Law School, the Government Law Center or any licensor is engaged in providing legal advice by making these materials available and the materials should, therefore, not be taken as providing legal advice.

All readers or users of these materials are further advised that the statutes, regulations and case law discussed or referred to in these materials are subject to and can change at any time and that these materials may not, in any event, be applicable to a specific situation under consideration. The information provided in these materials is for informational purposes only and is not intended to be, nor should it be considered to be, a substitute for legal advice rendered by a competent licensed attorney or other qualified professional. If you have any questions regarding the application of any information provided in these materials to a particular situation, you should consult a qualified attorney or seek advice from the government entity or agency responsible for administering the law applicable to the particular situation in question.

What Do We Do About Rebates?

One of the major topics affecting horse racing in the past decade has been the issue of rebates given to bettors.¹ In short, rebates are discounts off the takeout rate given to bettors. Pioneered by Las Vegas casinos in the mid 1990's, they initially attracted people looking for a break when the New York Racing Association increased its takeout in 1995.² Nevada formally outlawed rebates in 1997,³ and as a result of this legislation, rebate shops expanded broadly throughout America, to Indian reservations, and to off-shore betting shops. It has become an article of faith that every major bettor in American pari-mutuel wagering has been solicited by rebate shops, and the recruitment efforts of the rebate shops have proven especially attractive. Who wouldn't want to get more bang from their gambling bucks? Who wouldn't want a 50% discount off the retail price of a bet?

If takeout at an average American takeout is 20%, the rebaters are likely to give between 5% and 12% back to their major bettors. This in many cases is the difference between success at the races and total failure. While much of the rebate world exists in a shroud, there has been some limited public disclosure of the rebate process at work in North Dakota.⁴ In that state, the OTB operations were run by Racing Services, Inc. Racing Services was well known throughout the industry for rebating funds to its major bettors. However, in 2003, it was forced into receivership due to unpaid taxes.⁵ Criminal investigations are still pending. Racing Services went from \$9 million in wagering handle in 1998 to \$214.5 million in 2002.⁶ One single bettor, Peter Wagner, allegedly was wagering \$130 million per year through Racing Services.⁷ Betting at rebates shops has become the major growth sector of the horse racing industry. It has also become the most controversial.

Proponents believe that it has the capacity to significantly increase handle in horse racing. Bettors who win or who lose far less are likely to increase the size and frequency of their bets. The rebate shops often argue that they have attracted bettors to horse racing who previously had little or no interest in the sport. The fact that big players can now win

¹ Matt Hegarty, "Tracks Say Rebates Steal High Rollers," Daily Racing Form, August 10, 2000; Matt Hegarty, "Where Cream Of Crop Bet, Win, Bet Again," Daily Racing Form, January 10, 2003.

² See Matthew McAllester, "Hijacked High Roller," Newsday, January 28, 1996, Pg. A05; Andrew Beyer, "Rebate Shops Gain Inside Track," Washington Post, August 16, 2000 Pg. D08.

³ NRS § 464.075 (2003), enacted L. 1997, ch. 663.

⁴ There has been some limited disclosure of the operation of Racing and Gaming Services in St. Kitts. According to the Daily Racing Form, handle at Racing and Gaming Services was \$564 million in 2002. With 120 clients, per capita average annual betting at Racing and Gaming Services was \$4.7 million. Hegarty, January 10, 2003 article, supra at n. 1.

⁵ Matt Hegarty, "North Dakota Seizes Offtrack Betting Firm," Daily Racing Form, August 21, 2003.

⁶ Janell Cole, "RSI Numbers Off By Millions," Fargo Forum, July 22, 2003; Mike Nowatzki, "Racing Services Inc.: Rebates To Gamblers Spur Growth," Fargo Forum, July 27, 2003.

⁷ Janell Cole, "Column: Big Bettor Unmasked," Fargo Forum, September 22, 2003. The Daily Racing Form suggests a higher figure for Wagner of \$160 million. See Matt Hegarty, "North Dakota Bet Firm Rose, Then Quickly Fell," Daily Racing Form, August 22, 2003.

money through skill, according to the rebaters's argument, has brought new life into the sport. Their mantra has been "New Blood and More Churn."

Many people believe that current takeout rates in horse racing are far too high and make certain that racing can never compete with casino gambling where the takeouts on slot machines and almost all casino games are less than 10%. Nor can horse racing compete with sports wagering where takeout is traditionally quite low. If you effectively lower the takeout through rebates, perhaps racing can compete with other forms of gambling.

Finally, why should racing be different than other industries? The Discover Card gives cash back on all purchases. Why can't a racetrack? Most every casino has a slots club which works as a rebate on wagers and rewards patron loyalty. Horse racing is a sport that has been derided for years for its lack of innovation. Why not try some free enterprise ingenuity in the form of rebates?

Opponents of rebates believe that it creates a two tier system in racing where only the average \$2 bettors pay more. They believe it ends the mutuality in the pari-mutuel system. Others also believe that horsemen and racetracks are regularly shortchanged by the rebate shops. A bet placed on-track in most locations might contribute 5% to purses and 10% to the racetrack. If, instead, that same bettor now calls into a rebate shop which conducts no racing of its own, it is likely that racing would be lucky to get 5% of that betting dollar as a simulcast fee.

This might be seen most clearly at New York City OTB. New York City OTB operates an account wagering services without any fees or surcharges to its bettors. The OTB systems in New York State have since their inception been accused of shortchanging the racing industry. Based on 2002 data, more than eight cents out of every dollar wagered at New York City OTB returns to the racing industry.⁸ If that same bettor now places an account wager through a rebate shop that is paying 4% or 5% to a racetrack for that racetrack's simulcast signal, the loss to the racing industry is considerable.

So the idea should be to devise a system of rebates that maximizes the benefits of rebates while minimizing their downside. We want a system that encourages innovation, increases handle, contributes to the overall benefit of the industry, and treats all players equally. Here are the principles that should apply.

1. Rebates should not be per se illegal. Rebates can stimulate handle, and they can bring new life into racing. In the existing horse racing market where prices (takeout rates) are largely established by government decree, rebates can bring innovation, flexibility and some market reality into the pricing of wagers.

⁸ New York State Racing and Wagering Board, 2002 Annual Report, Pg. 56
http://www.racing.state.ny.us/pdf/2002%20Annual%20Report_final.pdf

2. There should be few limitations on a racetrack offering rebates on its own races.
3. There is no reason for rebates to be limited to merchandise rewards. There is little distinction between merchandise and cash, and the successful rebate shops have shown that cash works best.
4. There should be full public disclosure of rebates. We ought to know who is rebating, how much money is being rebated, and what the terms of the rebates are.
5. As part of the public disclosure process, an organization that wishes to rebate bets made on another track's races must inform that other track and the horsemen at that track of its rebating policies. In that manner, if track management believes that contracting with the rebating firm will provide little benefit to its racing, it can disapprove the deal under the Interstate Horse Racing Act.⁹ The horsemen also maintain authority under the Interstate Horse Racing Act - through their ability to contract with the racetracks on simulcasts - to exercise some authority over rebates.¹⁰ Disclosing rebate policies to horsemen would allow the horsemen some say over whether a track could simulcast its races to a rebate operator. Even at NYRA, where the horsemen may not possess any authority over simulcasts pursuant to the Interstate Horse Racing Act, the horsemen can make their feelings known to the Racing and Wagering Board which can take the sentiments of the horsemen into consideration in determining whether to approve the contractual arrangement.¹¹ In this manner, the host tracks and their horsemen can make a reasoned judgment on whether to allow their races to be simulcast to a rebate shop. Under this system, with the racetracks and horsemen acting with full knowledge in their own best interest, rebates would contribute to the overall improvement of the industry.
6. To assure equal treatment of bettors, the determination of the size of rebates should be determined only by objective factors. A rebate shop should not be allowed to offer rebates to friends of prominent people in government, racetrack trustees, or to trainers and owners. All classes of people should be eligible for rebates. Instead, there should be three objective criteria that apply to the amounts offered in rebates: (a) the amount wagered by the patron, (b) the takeout on particular bets at the host track, and (c) the particular tracks or racing associations that host the bet.

⁹ 15 USC § 3004.(a) (1).

¹⁰ 15 USC §§3004.(a) (1) (A) and (B)

¹¹ 15 USC §§3004. (a) (1) (A) and 3004.(a) (2).

Under this scenario, rebates would work like the Discover Card. Everyone is eligible for the awards which insures all players equal access to awards. It makes sense that a Peter Wagner betting upwards of \$100 million per year should be able to get a larger percentage rebate than a \$2 bettor. A rebate operator ought to be able to alter the size of the rebate based on the takeout of the bet. Thus, a rebate operator might only want to offer a 5% rebate on a win bet at NYRA (where the takeout is 14%)¹² while offering a 20% rebate on a superfecta at Pocono Downs where the takeout is 35%.¹³

Similarly a rebate operator might wish to give a larger size rebate on its own races. An OTB in New York State might want to give higher rebates on races run within New York State. Magna Entertainment and/or Churchill Downs might want to give higher rebates on racetracks they own. An East Coast rebate operator might want to encourage late night wagering by giving higher rebates for evening races conducted at Los Alamitos in California or Portland Meadows in Oregon. As long as the criteria for the rebates are objective, they should be approved.

I have appended a draft rebate rule that would specifically be designed for New York State. It could easily be remodeled to serve as an example for all states.

Draft Rebate Rule

I Definitions

- (a) "**Guest association**" means a racetrack other than the host track, or an authorized off-track betting entity, receiving or accepting a wager on a race.
- (b) "**Host track**" means a licensed or enfranchised racetrack, at which a race meet of horses is conducted.
- (c) "**Rebate**" means the portion of the takeout awarded by the host track or guest association to bettors which is intended to reduce or refund all or a portion of the takeout to such bettors. It includes refunds to bettors on any portion or percentage of the full face value of a pari-mutuel wager, or increasing the payoff of, or paying a bonus on, a winning pari-mutuel wager. Rebates shall be defined broadly to include awards of merchandise, services (including meals, parking admission, seating and programs) free or reduced cost pari-mutuel wagers, and monetary awards.
- (d) "**Takeout**" means the total amount of money excluding breakage withheld from each pari-mutuel pool authorized by the law governing the host track.

¹² See Racing, Pari-Mutuel Wagering and Breeding Law, § 229.1(a).

¹³ 4 P.S. § 325.221.

II Rebates by New York State Entities A racing association, corporation, non-profit racing association or regional off-track betting corporation may offer rebates to bettors provided it:

- (a) fully discloses the extent of the rebate program to the board. Such full disclosure shall include disclosure of the monetary value of all awards rebated to bettors in the previous calendar year, and the terms and conditions governing the award of rebates to individual bettors for the upcoming calendar year.
- (b) if it wishes to award rebates on horse races conducted at a track other than one at which the it operates, it fully discloses the extent of the rebate program to the host track on whose races it which it wishes to award rebates and to the host track's representative horsemen's association. Such full disclosure shall include disclosure of the monetary value of all awards rebated to bettors in the previous calendar year, and the terms and conditions governing the award of rebates to individual bettors for the upcoming calendar year,
- (c) provides assurances that only three criteria determine the amounts governing the rebate (1) the amount wagered by the bettor, (2) the takeout on the bet established at the host track, and (3) the particular racetrack or racing association where the horse race that was the subject of the bet was run, and
- (d) maintains, for a minimum of three years, a complete record of all wagers that are the subjects of the rebate.

III Rebates by Out-of-State Entities (a) The board shall approve: (1) all interstate and international simulcasting agreements and (2) all agreements authorizing an international or inter-state common pooling agreements, on a race or races to be conducted by a host association within the state. The guest association shall disclose to the board any agreement to award rebates to its bettors on races conducted by the host track.

(b) If the guest association does award rebates, such agreement shall only be approved by the board if the guest association:

- (1) fully discloses the extent of the rebate program to the board. Such full disclosure shall include disclosure of the monetary value of all awards rebated to bettors in the previous calendar year, and the terms and conditions governing the award of rebates to individual bettors for the upcoming calendar year.
- (2) provides assurances that only three criteria determine the amounts governing the rebate (i) the amount wagered by the bettor, (ii) the takeout on the bet established at the host track, and (iii) the particular racetrack, racetracks, or racing association where the horse race that was the subject of the bet was run, and
- (3) has fully disclosed the extent of the rebate program to the host track on whose races it which it wishes to award rebates, and to the host track's representative horsemen's association. Such full disclosure shall include disclosure of the monetary value of all awards rebated to bettors in the previous calendar year, and the terms and conditions governing the award of rebates to individual bettors for the upcoming calendar year.

- (4) maintains, for a minimum of three years, a complete record of all wagers that are the subjects of the rebate.