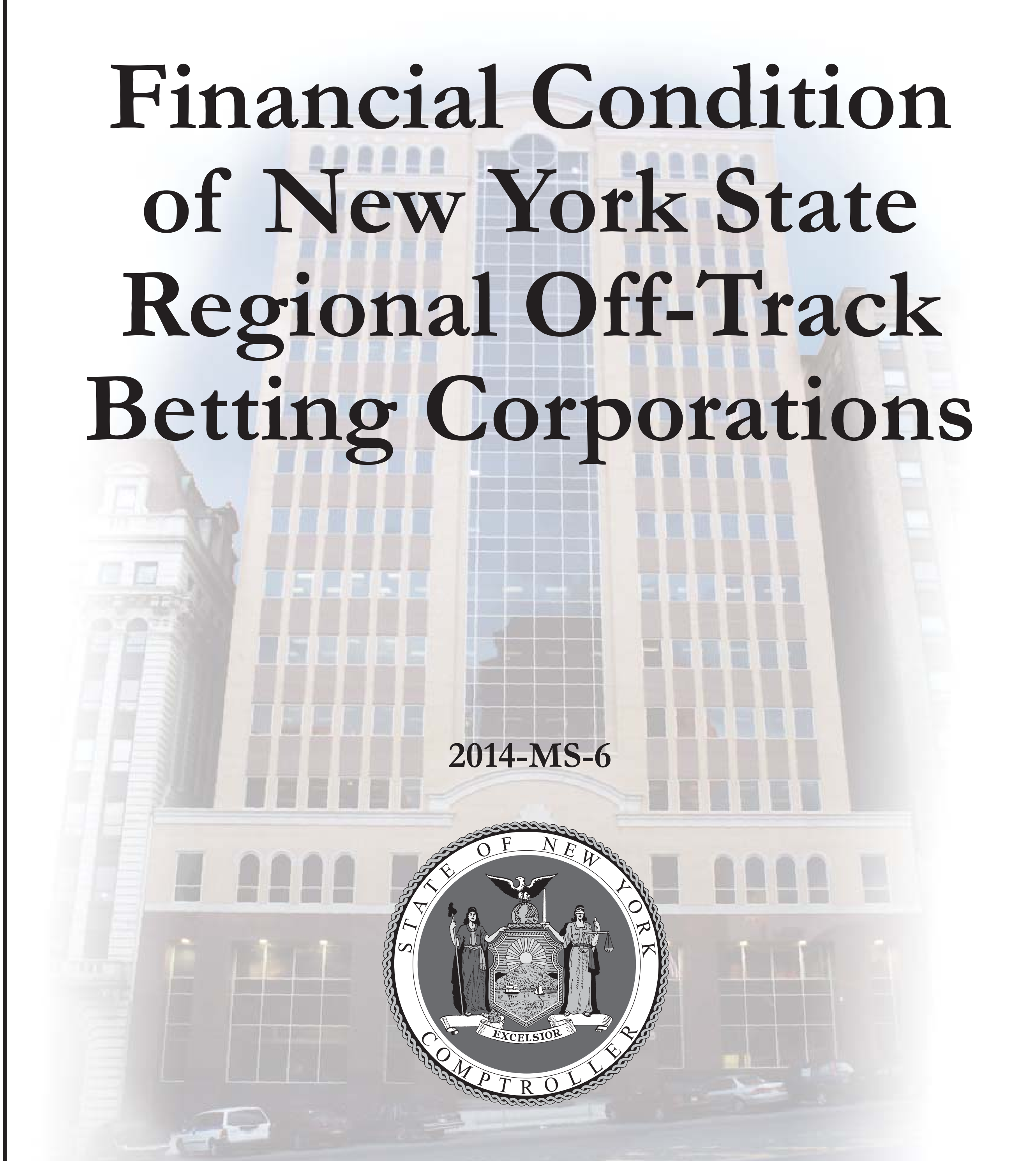
Office of the New York State Comptroller

Division of Local Government & School Accountability

Financial Condition of New York State Regional Off-Track Betting Corporations



2014-MS-6

Thomas P. DiNapoli

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State of New York
Office of the State Comptroller

Division of Local Government and School Accountability

September 2015

Dear Corporation Officials:

A top priority of the Office of the State Comptroller is to help local government officials manage government resources efficiently and effectively and, by so doing, provide accountability for the revenues and expenditures related to local government operations. The Comptroller oversees the fiscal affairs of local governments statewide, as well as compliance with relevant statutes and observance of good business practices. This fiscal oversight is accomplished, in part, through our audits, which identify opportunities for improving operations and Board of Directors governance. Audits also can identify strategies to reduce costs and to strengthen controls intended to safeguard local government assets.

Following is a report of our audit, entitled Financial Condition of New York State Regional Off-Track Betting Corporations. This audit was conducted pursuant to Article V, Section 1 of the State Constitution and the State Comptroller's authority as set forth in Article 3 of the New York State General Municipal Law.

This audit's results and recommendations are resources for Corporation officials to use in effectively managing operations and in meeting the expectations of their constituents. If you have questions about this report, please feel free to contact the local regional office for your county, as listed at the end of this report.

Respectfully submitted,

Office of the State Comptroller
Division of Local Government
and School Accountability

State of New York
Office of the State Comptroller
EXECUTIVE SUMMARY

Articles V and VI of the New York State Racing, Pari-Mutuel Wagering and Breeding Law (Racing Law), enacted in 1970 and 1973, authorize local governments in New York State to operate systems of off-track pari-mutuel betting as a method of raising revenues for local governments, the State's horse racing industry and New York State. The legislation was also intended to prevent and curb unlawful bookmaking and illegal wagering on horse races and ensure that off-track betting (OTB) activities were conducted in a manner compatible with the well-being of the State's horse racing industry.

Pursuant to the legislation, six regional OTB corporations (Corporations) were created as public benefit corporations: Capital, Catskill, Nassau, New York City, Suffolk and Western. Currently only five corporations remain, after the bankruptcy and subsequent closing of the New York City Corporation in 2010. Each remaining Corporation is governed by a Board of Directors whose members are appointed by the governing bodies of the relevant local governments.

Declining handle, or the total amounts wagered on horse races, has become a long-term trend for the Corporations. For the five-year period from 2009 through 2013, the five Corporations collected almost $3.7 billion in handle. This amount is down $1.2 billion (24 percent) from the $4.9 billion collected during the five-year period from 2004 through 2008,[1] a period over which the Corporations also experienced regular declines.

The Corporations do not retain the majority of the handle. Winning bettors receive a major percentage (77 percent) of the total handle wagered on each race. From the remaining handle, the Corporations then make monthly statutory distributions to the State's horse racing industry and the State and pay monthly surcharge fees to local governments participating in the OTB system. The amount remaining after statutory distributions and surcharges are paid constitutes the Corporations' operating revenues. From these, the Corporations then pay fees to tracks broadcasting races, as well as OTB operating expenses. Any remaining funds (net operating revenues) are then distributed to participating local governments.

Scope and Objective

The objective of our audit was to assess the financial condition of the five regional Corporations for the period January 1, 2009 through August 31, 2014. Our audit addressed the following question:

[1] *Financial Condition of New York State Regional Off-Track Betting Corporations (2009-MS-10)*

- Has the financial condition of the Corporations continued to deteriorate and have officials developed and implemented plans to benefit the Corporations' financial condition?

Audit Results

The financial condition of the Corporations has continued to deteriorate over the course of the last several years. Total handle for the Corporations declined almost 19 percent between 2009 and 2013 and the downward trend is continuing. In the first six months of 2014, handle fell by 7.5 percent when compared to the same period in 2013. Over the five-year period, the Corporations paid more than 48 percent of the handle remaining after compensating bettors in statutory payments to the racing industry and the State and local governments. Although most of the Corporations reduced their operating expenses during the five-year period, the Corporations' net operating revenues – their collective bottom line profit or loss – declined by $12.4 million due to the combination of the declining handle and "upfront" payments made to the racing industry and governments.

External conditions continue to have an effect on the Corporations' deteriorating financial condition. Over the past five years, the total amount bet on horse racing nationwide has declined 11.4 percent, from $12.3 billion in 2009 to $10.9 billion in 2013. The Corporations also compete for declining handle dollars with other gaming entities (e.g., casinos and Internet gaming sites), as well as with out-of-state advance deposit wagering companies that are neither regulated by, nor pay distributions to, the State.[2]

The Corporations have implemented recommendations previously made by the Office of the State Comptroller[3] in an effort to increase handle in a cost-effective way. The Corporations closed underperforming branches, expanded online and telephone wagering operations and increased the number of low-cost remote wagering locations. The Corporations have worked to control costs, with four of the five Corporations achieving a decrease in operating expenses over the five-year period reviewed. However, all these changes have not increased the handle or net operating revenues of the Corporations.

Further, certain amounts the Corporations are required to pay by statute, such as fees to enable OTBs to accept wagers on nighttime races, have added to the Corporations' cost burden over the years. The expectation was that the Corporations would realize additional handle from the nighttime races to offset the added statutory costs, which are based on 2002 total handle amounts. Total handle, however, has declined 67 percent since 2002. Therefore, the increase in revenue has not been realized and, as a result, has negatively impacted the Corporations. For example, Capital OTB officials stated that they are paying Saratoga Harness approximately $2.5 million annually as required by law, while the net revenue generated from these additional races amounts to only about $300,000 annually.

Additional external constraints limit the Corporations' ability to increase handle and improve their financial condition. For example, the Corporations must broadcast races from tracks throughout the United States and Canada to generate additional handle. In an effort to control costs, the Corporations have worked together to negotiate the fees paid to these tracks, but they say they have little bargaining power. Track rates have increased significantly between 2009 and 2013, with some tracks increasing rates 300 percent for the period.

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[2] The State enacted legislation in 2014 to require out-of-state advance deposit wagering companies to pay a fee that would go to the Corporations.

[3] See supra, note1.

Without significant changes to the statutory environment the Corporations must operate within, the long-term viability of their financial operations is questionable.

Comments of Corporation Officials

The results of our audit and recommendations have been discussed with Corporation officials and their comments, which appear in Appendix A, have been considered in preparing this report.

Introduction

Background

Articles V and VI of the New York State Racing, Pari-Mutuel Wagering and Breeding Law (Racing Law), enacted in 1970 and 1973, authorize local governments in New York State to operate systems of off-track pari-mutuel betting as a method of raising revenues for local governments, the State's horse racing industry and New York State. The legislation was also intended to prevent and curb unlawful bookmaking and illegal wagering on horse races and ensure that off-track betting (OTB) activities were conducted in a manner compatible with the well-being of the State's horse racing industry.

Pursuant to the legislation, six[4] regional OTB corporations (Corporations) were created. The New York State Racing and Wagering Board (Racing Board) has jurisdiction over the Corporations, along with all other horse racing activities and pari-mutuel betting activities in the State.[5] The five regional OTB Corporations remaining in operation are Capital, Catskill, Nassau, Suffolk and Western.[6] The New York City Corporation closed in 2010 after declaring bankruptcy. As provided for under the authorizing legislation, each of the remaining Corporations is a public benefit corporation governed by a Board of Directors whose members are appointed by the governing bodies of the relevant local governments.

The Corporations offer off-track pari-mutuel wagering on thoroughbred and harness horse races held at various racetracks in the State, as well as at racetracks located outside the State that have simulcast contracts with the Corporations. The Corporations accept wagers at various physical locations, as shown in Figure 1, as well as over the phone and via the Internet.

Figure 1: OTB Wagering Locations (as of 2014)

Corporation	Branches	Remote Wagering Locations	Tele-theater
Capital	33	31	2
Catskill	19	12	1
Nassau	6	13	1
Suffolk	5	34	1
Western	26	27	0
Total	**89**	**117**	**5**

4 The legislation authorized seven Corporations, yet only six were actually created.

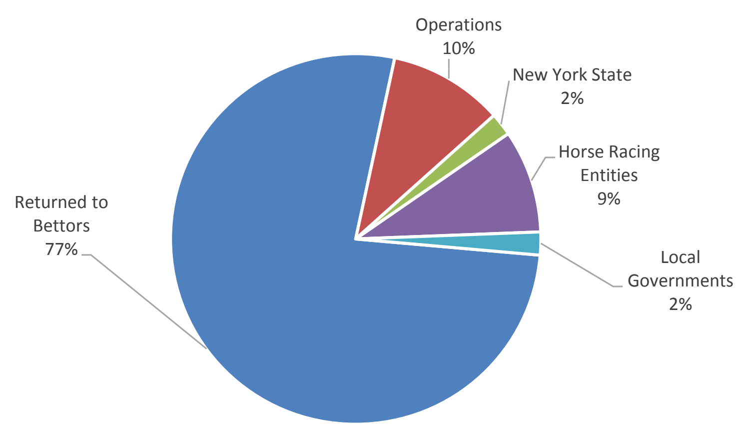
5 In 2013, the Racing Board was merged with the New York State Division of Lottery and other agencies to create the New York State Gaming Commission. For additional information see the Horse Racing section of the Gaming Commission's website at www.gaming.ny.gov/horseracing.

6 Western also owns and operates the Batavia Downs Gaming facility, which conducts live harness racing and simulcasts races to and from other racetrack facilities. In addition, Western offers video gaming operations.

Declining handle, or the total amounts wagered on horse races, has become a long-term trend for the Corporations. For the five-year period from 2009 through 2013, the five Corporations collected almost $3.7 billion in handle.[7] This amount is down $1.2 billion (24 percent) from the $4.9 billion collected during the five-year period from 2004 through 2008, a period over which the Corporations also experienced regular declines. Further, the downward trend appears to be continuing – for the first six months of 2014 the handle dropped by 7.5 percent when compared to the same period for 2013.

The Corporations do not retain the majority of the handle. Winning bettors receive 77 percent of the total handle wagered on each race.[8] From the remaining handle, the Corporations then make monthly statutory distributions to the State's horse racing industry and to the State, and pay monthly surcharge fees to local governments that participate in the OTB system. The handle that remains after statutory distributions and surcharges are paid plus other miscellaneous revenues constitutes the Corporations' operating revenues. From these operating revenues, the Corporations then pay fees to tracks that broadcast races, as well as operating expenses incurred to operate the OTB. Any remaining funds (net operating revenues) are then distributed to participating local governments. Figure 2 details the distribution of a wager once received by the Corporations.

Figure 2: Breakdown of $1 Wager



7 As presented in this report, the term handle is synonymous with the term "net handle" as used in the Racing Board's Annual Report and Simulcast report.

8 Due to varying presentations of surcharges, other revenues and capital acquisitions, the amount of handle can be shown as totaling from 75 percent to 77 percent. The Corporations' CPA reports show the amount of handle returned to betters totaling 77 percent.

The Corporations retain, on average, 10 cents on each dollar wagered to fund their day-to-day operations, including the contractual fees for broadcasting races.

Objective

The objective of our audit was to assess the financial condition of the five regional Corporations for the period January 1, 2009 through August 31, 2014. Our audit addressed the following question:

- Has the financial condition of the Corporations continued to deteriorate and have officials developed and implemented plans to benefit the Corporations' financial condition?

Scope and Methodology

For the period January 1, 2009 through August 31, 2014, we interviewed Corporation officials, reviewed the Racing Law, examined Corporation records and reports and other documentation, and analyzed audited financial statements for the five years ending December 31, 2013. We also reviewed the Corporations' first six months of operations in 2014 in comparison to the same period during 2013 for handle generated by the Corporations.

We conducted our audit in accordance with generally accepted government auditing standards (GAGAS). More information on such standards and the methodology used in performing this audit are included in Appendix C of this report.

Comments of Corporation Officials

The results of our audit and recommendations have been discussed with Corporation officials and their comments, which appear in Appendix B, have been considered in preparing this report.

Financial Condition

The Corporations' financial condition determines their ability to continue to make statutory and contractual payments, cover operating expenses and provide future revenue streams to participating local governments. The financial condition of the State's five regional Corporations has continued to deteriorate over the last several years. Total handle for the Corporations declined by almost 19 percent between 2009 and 2013;[9] further, in the first six months of 2014, handle fell by 7.5 percent when compared to the same period in 2013.

There are many reasons for the Corporations' declining handle and deteriorating financial condition. Over the past five years, the total amount bet on horse racing across the United States has declined 11.4 percent, from $12.3 billion in 2009 to $10.9 billion in 2013. In 2013, the total of horse racing wagers for the United States was down 0.1 percent compared to the prior year, while the Corporations' handle was down considerably more, at 5 percent. The Corporations also have to compete for gambling revenue with other entities in the gaming industry, such as casinos, video gaming and government-sponsored lotteries. In addition, the Corporations continue to contend with out-of-state advance deposit wagering (ADW) companies that collect wagers and provide payouts to gamblers without the statutory payments required of the Corporations.[10]

To further compound the issue, the Corporations have experienced dramatic increases in the rates charged by tracks broadcasting (simulcasting) horse racing. The Corporations' operating revenues, what remains after they make required payments and pay operating expenses, declined by a combined $12.4 million[11] between 2009 and 2013. Although the Corporations have implemented recommendations made by the Office of the State Comptroller (OSC) from a prior audit and have reduced some expenses, they have continued to experience fiscal decline.

Given the significant amount of "upfront" payments the Corporations must make to the racing industry and governments in an environment of declining handle, the Corporations may have trouble reducing expenses enough to ensure their long-term viability without legislative action.

9 See Appendix A, Figure 9 for additional detail.

10 The State enacted legislation in 2014 to require out-of-state ADW companies to pay a fee that would go to the Corporations.

11 See Figure 7 for additional detail.

Decline in Handle

All five Corporations have experienced an overall decline in handle over the five-year period 2009 through 2013, which collectively amounted to a decline of approximately $153 million[12] or nearly 19 percent. Among the Corporations, Suffolk experienced the greatest percentage decline, down 29 percent. It also experienced the largest average annual decline at $8.8 million. Further, from January through June 2014 each Corporation's handle was down 7.5 percent compared to the same period in 2013, as shown in Figure 3.

Figure 3: Decline in OTB Handle[a] – Comparison of June 2013 to June 2014

	January – June 2013	January – June 2014	Difference	% Change
Capital	$75,438,653	$71,855,984	($3,582,669)	(4.8%)
Catskill	$46,634,426	$41,419,734	($5,214,692)	(11.2%)
Nassau	$114,118,825	$103,404,346	($10,714,479)	(9.4%)
Suffolk	$56,055,317	$53,224,502	($2,830,815)	(5.1%)
Western	$49,837,288	$46,690,399	($3,146,889)	(6.3%)
Total	**$342,084,509**	**$316,594,965**	**($25,489,544)**	**(7.5%)**

[a] Total handle before paying winning bets.

Decline in Operating Revenues

As shown in Figure 2, the majority of the Corporations' handle is returned to bettors. The Corporations' remaining handle after paying bettors, called racing and gaming revenues,[13] totaled about $925 million for the five-year period. To calculate total operating revenues, the Corporations' racing and gaming revenues are reduced by statutory distributions paid to the racing industry and the State and by surcharges paid to local governments with tracks, before adding in other miscellaneous revenues.

Statutory Distributions and Upfront Surcharges[14] – Statutory distributions and upfront surcharges represent a significant financial outlay for the Corporations. During the five years ended December 31, 2013, the Corporations paid almost $407.2 million for statutory distributions and surcharges, as shown in Figure 4. Of this amount, $19.6 million was for legally required monthly distributions to Counties with racetracks, and $387.5 million was distributed for statutorily required payments.

[12] See Appendix A, Figure 9 for additional detail.

[13] Reported racing and gaming revenues do not include revenues from video gaming and live racing activities.

[14] The upfront surcharges referenced in this section are distributed to New York State counties with tracks.

Figure 4: Total Statutory Distributions and Surcharges Paid to Counties with Tracks[a]						
	2009	2010	2011	2012	2013	Total
Capital	$19,482,082	$18,234,426	$17,789,320	$18,275,909	$17,920,937	**$91,702,674**
Catskill	$12,184,235	$11,423,290	$11,207,100	$11,268,561	$10,330,690	**$56,413,876**
Nassau	$27,305,038	$24,676,380	$28,320,023	$25,547,046	$24,998,962	**$130,847,449**
Suffolk	$15,924,417	$14,600,475	$13,233,567	$12,566,829	$12,259,473	**$68,584,761**
Western	$13,495,491	$12,601,917	$12,011,625	$11,191,676	$10,311,172	**$59,611,881**
Total	**$88,391,263**	**$81,536,488**	**$82,561,635**	**$78,850,021**	**$75,821,234**	**$407,160,641**

[a] These figures exclude the video gaming and live racing component of Western.

The majority of the amounts paid in statutory distributions (78 percent) were payments to the racing industry totaling $318.9 million. Distributions to racing entities are made to:

- In-state racetracks based on statutory rates depending on the type of wager and other contractual agreements,
- Out-of-state racetracks based on specific contractual agreements and
- Certain horse breeding funds created to support and promote in-state horse breeding and racing.

Among the payments made to in-state racetracks are those made to harness tracks in conformance with New York State's "Hold Harmless" law enacted in 2003. This law authorized the Corporations to accept wagers on nighttime[15] thoroughbred racing. In return, the Corporations were required to pay in-state regional harness tracks a percentage of their handle to compensate them for lost bets plus other "Maintenance of Effort" payments. The Racing Board calculates the amount the Corporations must pay harness tracks based on 2002 total handle figures of $2.04 billion.[16] Although wagers on nighttime races were expected to generate additional handle for the Corporations, the increase was not realized; in fact, total handle has declined to $664 million (67 percent).[17] The costs the Corporations have to bear under this law significantly outweigh the benefits received. For example, Capital OTB officials stated that they are paying Saratoga Harness approximately $2.5 million annually as required by law, while the net revenue generated from these additional races amounts to only about $300,000 annually.

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[15] Post times after 7:30 p.m.

[16] As reported in the *2002 Annual Report and Simulcast Report* of the Racing Board. Total handle includes handle from the New York City OTB until 2010 when it filed for bankruptcy, which partially skews the percentages over the period.

[17] Total handle in 2013 – see Appendix A, Figure 9 for more information.

Also included in the statutory distributions are payments to New York State for pari-mutuel taxes and breakages,[18] regulatory fees to the Racing Board and uncashed tickets. Capital and Western also make contractual payments to the Cities of Albany and Niagara Falls,[19] in lieu of paying other local taxes.

Operating Revenue – All five Corporations' total operating revenues decreased between 2009 and 2013, by $28.6 million (24 percent), from $119.3 million to $90.7 million, as shown in Figure 5. Figure 6 shows that Suffolk experienced the most significant decline in operating revenue, a 34 percent decline from $21.9 million in 2009 to $14.4 million in 2013. Nassau experienced the smallest decline at 17 percent, or $6 million.

Figure 5: Total Operating Revenues 2009-2013

	2009	2010	2011	2012	2013	Total
Racing and Gaming Revenues	$207,659,066	$190,549,416	$186,188,256	$174,202,564	$166,518,221	**$925,117,523**
Less: Statutory Distributions and Upfront Surcharges	$88,391,263	$81,536,488	$82,561,635	$78,850,021	$75,821,234	**$407,160,641**
Operating Revenues	$119,267,803	$109,012,928	$103,626,621	$95,352,543	$90,696,987	**$517,956,882**

Figure 6: Operating Revenues by Corporation, 2009-2013

	2009	2010	2011	2012	2013	% Change 2009-2013
Capital	$25,651,136	$22,550,444	$20,419,250	$19,493,243	$18,662,586	(27%)
Catskill[a]	$16,447,576	$15,078,463	$14,676,196	$14,294,312	$12,916,446	(21%)
Nassau	$35,694,098	$33,349,242	$34,962,652	$31,148,646	$29,684,166	(17%)
Suffolk	$21,947,592	$19,765,651	$16,769,928	$14,709,154	$14,385,373	(34%)
Western[b]	$19,527,401	$18,269,128	$16,798,595	$15,707,188	$15,048,416	(23%)
Total	**$119,267,803**	**$109,012,928**	**$103,626,621**	**$95,352,543**	**$90,696,987**	**(24%)**

[a] Operating revenue includes other non-operating revenue, which is presented differently in the audited financial statements.
[b] OTB operations only. Amounts exclude video gaming and live racing activities.

Decline in Net Operating Revenues

The Corporations' net operating revenues – operating revenues less operating expenses – constitute their collective bottom line profit or loss and a measure of their overall financial viability. The Corporations' bottom line dropped by $12.4 million over the five-year period, as shown in Figure 7, even though they reduced total operating expenses.

[18] To avoid bettor payouts in pennies, "breakage" was developed as a method of rounding off a bettor's winnings by reducing the payout to an amount set by statute.

[19] Pursuant to Racing Law, Capital and Western have contractual agreements with the Cities of Albany and Niagara Falls, respectively, whereby each City receives 1 percent of the tele-theater handle in these locations in lieu of any other local tax. Western's tele-theater closed in 2012.

Figure 7: Net Operating Revenue/(Loss) 2009 - 2013						
	2009	2010	2011	2012	2013	Change from 2009-2013
Capital	$4,461,728	$2,145,578	($150,705)	$1,141,728	$1,006,260	($3,455,468)
Catskill	$4,294,189	$3,495,614	$2,832,945	$2,752,723	$1,628,673	($2,665,516)
Nassau	$1,125,073	($136,299)	$11,942,294	$1,165,203	($2,679,097)	($3,804,170)
Suffolk	($2,908,224)	($2,998,997)	($3,799,335)	($2,597,776)	($2,995,590)	($87,366)
Western[a]	($297,483)	($1,378,605)	($2,106,315)	($1,705,780)	($2,695,530)	($2,398,047)
Total	**$6,675,283**	**($1,127,291)**	**$8,718,884**	**$756,098**	**($5,735,284)**	**($12,410,567)**

[a] OTB operations only. Amounts exclude video gaming and live racing activities.

The Corporations' operating expenses declined by 9 percent overall during the 2009 through 2013 period. Four Corporations cut their operating expenses: Capital by $3.5 million, Catskill by almost $800,000, Nassau by over $3.2 million and Suffolk by $7.7 million. Only Western experienced an increase in operating expenses (by more than $3.7 million); however, this was the result of all of Western's operations, not just the OTB operations.[20]

Operating Expenses – Track Compensation – In order to collect wagers on races, the Corporations must have a product to broadcast. Therefore, they must contract with the providers of the races. The Corporations enter into agreements with tracks throughout the United States and Canada to simulcast the races run at these tracks. In exchange for allowing the Corporations to broadcast these races, the Corporations pay the hosting tracks a fee, which is based on the handle wagered for the race. Between 2009 and 2013, the Corporations have experienced dramatic increases in the fees paid for these track contracts. During this time, the Corporations worked together to negotiate the track rates; however, Corporation officials say they have little bargaining power. Some track rates increased 300 percent for the period.

In addition, when the Corporations provide ADW and take Internet wagers, they must pay an additional fee to the hosting tracks. Most significantly, the fee for hosting the Indiana Downs races increased 300 percent from 1.5 percent in 2009 to 6 percent in 2013 for ADW wagers placed. This means that for every $100 wagered on races at Indiana Downs, the Corporations must pay the track $6 in fees. Corporation officials say they have trouble controlling these increased expenses.[21] If they do not contract with the tracks, they have no races to broadcast and, therefore, no product to offer to their customers. The increased costs associated with these track contracts have decreased the net operating revenues of the Corporations.

[20] Operating expenses for the OTB operation alone have decreased about $2.1 million (10 percent) over the five-year period. See Appendix A for information about Western's video gaming and live racing revenues.

[21] Racing Law only limits the fees that can be charged for races run as part of the Triple Crown and the Breeders' Cup.

Distributions to Participating Local Governments – Local governments receive monthly distributions from their respective regional OTB. These distributions represent the allocation of surcharge revenues collected from winning bettors as well as the distribution of net operating revenue based on the operating results of the OTB. The decline in operating revenues, despite the Corporations' cost cutting, has reduced distributions to local governments. As a result, the Corporations have a reduced ability to function as intended as public benefit corporations. The distributions to participating local governments have declined 42 percent to nearly $10.2 million in 2013, with the most significant reduction being a 69 percent decline (almost $3.2 million) in Catskill. Figure 8 shows the distributions to local governments made by the Corporations from 2009 to 2013.

Figure 8: Distributions to Participating Local Governments

	2009	2010	2011	2012	2013	Change	% Decline 2009 - 2013
Capital	$3,665,470	$4,416,130	$2,567,525	$2,341,415	$2,124,207	($1,541,263)	(42%)
Catskill	$4,612,696	$3,749,061	$2,736,569	$2,879,591	$1,430,267	($3,182,429)	(69%)
Nassau	$3,572,790	$3,137,476	$3,290,558	$2,971,761	$2,805,880	($766,910)	(21%)
Suffolk	$2,013,385	$1,724,051	$1,480,176	$1,313,678	$1,207,759	($805,626)	(40%)
Western	$3,750,116	$3,040,412	$2,729,044	$2,440,822	$2,596,372	($1,153,744)	(31%)
Total	**$17,614,457**	**$16,067,130**	**$12,803,872**	**$11,947,267**	**$10,164,485**	**($7,449,972)**	**(42%)**

The many issues that the Corporations are facing, including the statutory payment requirements, downturn in racing interest and significant out-of-state track fee increases, have all contributed to the continued decline of their financial standing. Continuation of these trends will affect not only the Corporations' operations, but also the local governments that receive related distributions.

Implementation of Previous Recommendations

During our prior audit,[22] recommendations were made regarding both action to be taken by the Corporations and by State Policymakers. While the recommendations to State Policymakers did not yield any changes in the formulary by which the Corporations distribute the funds collected from placed wagers, the Corporations did take action. For example, the Corporations implemented an innovative practice of negotiating collectively for track rates to try and improve their bargaining power. In addition, the Corporations made improvements in betting locations and methods.

Branch and Betting Locations – While the Corporations' branch operations generate OTB handle, many individual locations also have generated operating losses. For example, all seven Nassau branch locations lost money in 2013, with the largest loss of just over $1 million being generated by the Green Acres location. The

[22] See supra, note 1.

Corporations also operate remote locations, which vary in name – EZ Bet, Fast Track or Qwik Bet. They operate similarly, but at lower costs than branch locations. These remote locations are wagering terminals placed in other businesses (e.g., restaurants, bars and newsstands), allowing bettors to place OTB wagers without having to go to a branch location. Since the last audit, the Corporations have increased remote wagering locations, from 77 to 117 locations throughout the State (52 percent). While locations such as Suffolk's Jon Thomas Inn generated a net gain of $688,000, nine remote wagering locations had operating losses in 2013. The most significant operating loss was Catskill's Norwich location, which generated a net loss of $17,557 in 2013.

We commend the Corporations for taking steps to reduce the number of low performing branch locations as recommended. In total, the Corporations have reduced their branch locations from 124 locations in 2009 to 89 in 2014, a 28 percent decrease.[23] Although this has reduced the operating costs of the Corporations, it has done little to stem the downturn in handle.

Online and Telephone Wagering – As recommended, the Corporations have expanded online and telephone wagering. For example, in 2009, only Capital and Nassau had Internet wagering, but all five regional Corporations were operating Internet wagering systems by the end of 2013. We commend the Corporations for taking steps to expand telephone and Internet services, but these improvements have not generated an increase in wagers placed.

Recommendations

The Corporations Boards' should continue:

1. To explore cost cutting measures.

2. Efforts to increase revenues through innovative marketing.

3. To analyze the cost/benefit of branch and remote locations.

4. To negotiate collectively for track rates.

State Policymakers should:

5. Review the formula used to calculate the Corporations' payments to harness tracks, as required by the 2003 Hold Harmless law.

[23] The total amount saved from the reduction in the number of branch locations could not be separated from the increases incurred to open and operate additional remote locations.

6. Consider examining the formulas used to calculate the Corporations’ upfront statutory and surcharge payments to balance the State's revenue objectives with the Corporations' financial viability.

APPENDIX A

ADDITIONAL FINANCIAL INFORMATION

Figure 9: OTB Handle[a] by Corporation: 2009 – 2013

	2009	2010	2011	2012	2013	Total	2009 to 2013 Period Decline	2009 to 2013 Percentage Decline
Capital	$176,566,467	$165,688,551	$156,960,633	$159,563,685	$153,656,891	$812,436,227	$22,909,576	(13%)
Catskill	$107,401,445	$99,604,857	$98,021,201	$97,613,210	$87,654,538	$490,295,251	$19,746,907	(18%)
Nassau	$257,581,744	$235,993,822	$257,074,414	$229,698,269	$219,492,548	$1,199,840,797	$38,089,196	(15%)
Suffolk	$153,501,836	$139,052,540	$122,693,944	$113,311,268	$109,200,645	$637,760,233	$44,301,191	(29%)
Western	$121,882,680	$114,037,661	$106,031,058	$98,840,851	$94,245,876	$535,038,126	$27,636,804	(23%)
Total	**$816,934,172**	**$754,377,431**	**$740,781,250**	**$699,027,283**	**$664,250,498**	**$3,675,370,634**	**$152,683,674**	**(19%)**

[a] Total handle before paying winning bets.

Figure 10: Western OTB Corporation's Total Racing and Gaming Handle[a]

	2009	2010	2011	2012	2013
Corporate and Branch Operations	$121,882,680	$114,037,661	$106,031,058	$98,840,851	$94,245,876
Batavia Downs	$7,363,314	$6,955,322	$6,776,826	$7,139,914	$6,080,417
Video Gaming	$419,540,825	$429,634,724	$473,755,412	$547,263,631	$566,510,901
Total	**$548,786,819**	**$550,627,707**	**$586,563,296**	**$653,244,396**	**$666,837,194**

[a] For the purposes of this report, we did not include Western's video gaming and live racing handle revenues in our calculations. They are presented here for the reader's information.

APPENDIX B

RESPONSES FROM CORPORATION OFFICIALS

We provided a draft copy of this global report to the five OTB's we audited and requested responses. We received response letters from all OTBs.

The OTBs coordinated their responses and collectively had areas of concern regarding the future of OTBs due to the declining handle and statutory regulations placed on them. The following comments were excerpted from the responses.

Overall Comments

Nassau OTB – "Although the recommendations in the 2009 audit were implemented, Nassau OTB continues to experience significant decline in revenue. The current antiquated and inequitable statutory model must be changed to allow the Corporations to be able to fulfill their primary purpose of providing much needed revenues to their municipalities. We implore the State Legislature and Governor's office to review the findings and adopt the positive solutions offered therein and herein for the benefit of the taxpayers served by these public benefit corporations."

Suffolk OTB – "We urge the State Legislature and the Governor to review the findings outlined in the State Comptroller's audit and adopt the recommendations outlined by the five Regional Off-Track Betting Corporations in addition to our recommendations to amend the ADW law. These recommendations will address the antiquated and inequitable statutory requirements and bring NYS in line with other racing jurisdictions, level the playing field and enable the Corporations to eliminate operating deficits, distribute local funds to local governments and fulfill our mission."

Capital OTB – "Capital OTB's management and its Board of Directors believe that the issues discussed in the report outline the relevant circumstance (economic fluctuations, competition, restrictions for siting remote wager locations and the statutory distributions and surcharges that represent a significant financial outlay for the Corporation) that have resulted in the financial decline within the State's OTBs."

Catskill OTB – "The New York Regional OTBs distributed over $57 million to the racing industry during 2013. OTBs do not lose money, but in fact, are required to distribute in excess of revenues received. With the legislative proposals presented, New York OTB can continue to operate for the benefit of ALL participants of OTB revenues."

Western OTB – "…Western OTB operations continue to decline as noted. The reasons for that decline are appropriately identified and explained within the audit findings, of particular note, the role of statutory distributions and track compensation in this decline are properly identified."

Advanced Deposit Wagering

Nassau OTB – "Nassau maintains that the statutes regarding multi-jurisdictional advance deposit wagering regulations need to be reexamined."

Suffolk and Nassau OTB – "In 2013, NYS passed legislation requiring out of state entities that accept wagers from NYS residents to pay a percentage of those wagers to NYS. The NYS Gaming Commission then shares those payments with tracks and the OTB Corporations to partially reimburse them for the lost revenue. Certain out of state entities, have "partnered" with New York State tracks to avoid making these payments."

Catskill OTB – "Penalties or prohibition should be legislated or regulated, for the out of state ADWs that increase fees over 2013 rates. In 2013 the Legislature acted to regulate ADW by requiring out of state operators of telephone and internet wagering to be licensed effective 2014, and to pay 5% on all wagers from New York residents, a portion of such to offset OTB regulatory fees. These out of state ADWs have since increased fees paid to them by 5% to offset their licensing fee." "…Protect the NY OTB market by imposing penalties or prohibiting collaboration with in state venues to circumvent ADW regulation."

Capital OTB – "Enforce legislation that passed in 2013, requiring out-of-state ADW sites to pay a surcharge on bets they take from New York residents. These surcharge dollars go to help support NY racetracks and OTBs. We want to make sure the State is doing everything possible to ensure that these sites are licensed and paying their fair share."

Statutory Payments and Other Legislative Suggestions

Western OTB – "It is obvious to us that the current statutory model must be altered to allow NYS OTBs to generate needed revenues to their municipalities. As noted on Page 4 of the Audit, "Without significant changes to the statutory environment the Corporations must operate within, the long-term financial viability of their financial operations is questionable."

Potential legislative changes that will positively address this circumstance are noted:

- Catskill, Capital and Western OTBs – Hold Harmless: "The elimination of such payments are needed as the current statute is based on outdated handle, that at times causes OTBs to pay to the harness tracks an excess above the actual handle OTB receives."

- Catskill OTB – "Allow OTBs to retain surcharge payable to non-participating counties where a track is located. The original purpose was to offset track admission taxes projected to decline with the onset of OTB. Tracks no longer charge admission, and local governments with tracks now benefit from Video Lottery Terminals (VLT) since operating at those tracks."

- Capital and Catskill OTBs – "Authorize an OTB operated VLT facility in each OTB region to provide for county taxpayer relief and more population centered facilities."

- Catskill OTB – "Expand OTB product offerings with on-line gaming, instant racing and/or sports wagering."

- Capital, Catskill and Western OTBs – "Allow OTB to retain uncashed ticket monies for corporate purposes."

- Catskill OTB – "Reduce pari-mutuel tax for OTBs."

- Catskill OTB – "Enforce OTB statutory rates caps on fees payable for out of state harness racing and special event thoroughbred racing."

- Capital OTB – "Reduce payments OTB Corporations make to New York racetracks (both harness and thoroughbred). New York tracks have been operating as casinos for many years and have generated tens, if not hundreds, of millions of dollars in revenues from their VLT operations. OTB monies that go to tracks, in our view, should be redirected to help fund county budgets and help county taxpayers. Legislature action should be taken to reduce or eliminate these payments to New York tracks/casinos."

- Catskill, Capital and Western OTB – "Eliminate the provision that allows harness tracks to deny placement of OTB branch sites. This provision gives harness tracks the ability to make OTB less efficient by denying less costly branch sitings."

APPENDIX C

AUDIT METHODOLOGY AND STANDARDS

We conducted this performance audit in accordance with GAGAS. Those standards require that we plan and perform the audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our findings and conclusions based on our audit objective. We believe that the evidence obtained provides a reasonable basis for our findings and conclusions based on our audit objective.

To complete the audit objective, we interviewed Corporation officials regarding budgeting practices and monitoring. We reviewed financial activity documents prepared by each Corporation's external accounting firms and financial information provided by each of the Corporations. We analyzed revenue, expense and gambling activity trends to reach our conclusions. We reviewed the applicable State laws governing OTB operations and track wagering.

We compiled data from all currently operating Corporations to create comparison and trend analysis of the operations across the State. We obtained published data for the national horse racing wagering trends for the audit scope period and compared these to the trends from the regional OTB operations.

APPENDIX D

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APPENDIX E

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