STATE OF CALIFORNIA

CALIFORNIA HORSE RACING BOARD

ROBERT BROWNING MILLER
GENERAL COUNSEL

ORDER

THE CALIFORNIA HORSE RACING BOARD HEREBY ADOPTS THE PROPOSED DECISION OF REFEREE C. SCOTT CHANEY IN THE MATTER OF THE COMPLAINT OF SAN LUIS REY RACING, INC., EFFECTIVE JULY 18, 2013.

DATED: JULY 18, 2013

KRIS BREED, EXECUTIVE DIRECTOR

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BEFORE THE

CALIFORNIA HORSE RACING BOARD

STATE OF CALIFORNIA

In the Matter of:	)	
Complaint of San Luis Rey Racing, Inc.	)	
(dba San Luis Rey Downs)	)	
	)	No Case Number
	)	
	)	

PROPOSED DECISION

PROCEDURAL BACKGROUND

On December 12, 2012, I was appointed by the California Horse Racing Board (hereinafter "CHRB" or "the Board") to serve as a Referee "for the purpose of taking evidence and rendering a Proposed Decision in the Matter of the Complaint of San Luis Rey Racing, Inc., (doing business as San Luis Rey Downs)." *See Exhibit A.* This appointment was made pursuant to CHRB rule 1414 (Appointment of Referee). Apparently, at some point prior to this appointment, San Luis Rey Downs, Inc. (hereinafter "SLRD") filed a civil suit and a complaint with the CHRB alleging , among things, violations of California Business and Professions code sections 19535 and 19607. Responding parties included, but were not limited to, Southern California Off-Track Wagering, Inc. (hereinafter "SCOTWINC"), Thoroughbred Owners of California (hereinafter "TOC"), Hollywood Park Racing Association & Hollywood Park Fall Racing Association (collectively hereinafter "Hollywood Park"), Los Angeles Turf Club (hereinafter "Santa Anita"), the CHRB itself, Del Mar Turf Club (hereinafter "Del Mar") and Fairplex Park (hereinafter "Fairplex"). Some responding parties have been dismissed from the civil suit for political or legal reasons and it appears that only SCOTWINC and Hollywood Park remain. However,

naming the exact parties is inconsequential (except to the parties themselves) to this inquiry as will be made clear in this proposed decision.

The instant civil matter centers around SLRD's allegations that the responding parties have violated California Business and Professions Code sections 19535 and 19607 (hereinafter "the code" or "the stabling and vanning laws"). Those code sections require that a stabling and vanning fund be established and distributed "pursuant to supervision of the [CHRB]." *Cal. B & P code sections 19607 and 19607.2*. Horse Racing Law further provides that "[u]pon request of any party within the organization, the board shall adjudicate any dispute regarding costs, or other matters relating to the furnishing of offsite stabling or vanning. The board may, if necessary, appoint an independent auditor to assist in the resolution of disputes. The auditor shall be reimbursed from the funds of the organization." *Cal. B & P section 19607.3(d).* In November 2012, pursuant to code section 19433, the CHRB did conduct its own audit, and although it cannot be characterized as "independent" as provided for under the stabling and vanning sections, an independent audit would have been limited by the same boundaries that the CHRB's audit revealed. While the audit noted that all payments were properly made and documented pursuant to the law, any audit would first have to contemplate what the law requires. The civil court judge in this matter has stayed the proceeding pending the CHRB's decision or recommendation because it is the body that regulates horse racing in general and is required to supervise these provisions specifically. The CHRB has appointed this referee to examine two specific issues in order to guide it in determining its position. Those issues are: "(1) Whether the Stabling and Vanning Funds, distributed pursuant to Business and Professions Code section 19607 et seq., have been properly allocated and (2) Whether the Audit Report, dated November 6, 2012, performed by the Audit Unit of the California Horse Racing Board, is in accordance with Business and Professions Code section 19433." *See Exhibit A*. The CHRB assignment gave me great freedom in determining how to proceed in this matter. To that end, an initial round of briefs was submitted by the complaining and responding parties. Next, I heard one day of oral arguments and an additional day of oral testimony by various witnesses called by each of the parties. Lastly, a final round of written briefs was submitted. SLRD was represented at all times by attorneys Kevin Carey and Patrick Webb. The responding parties were collectively represented by John Sturgeon and Jonathan Alon. The CHRB was represented by DAG Mike Early, although its participation was minimal. The following witnesses testified: LeAnn Howard, Martin Panza, Jack Liebau, Lou Raffetto, and Barabra Helm. All of the proceedings were recorded by court reporter Michelle Deirig.

LIST OF EXHIBITS

Exhibit A	CHRB Notice of Appointment of Referee (12 December 2012)
Exhibit B	Opening Brief of Claimant, San Luis Rey Racing. Doing Business as the San Luis Rey Sown Training Center
Exhibit C	First Amended Complaint and Petition for Writ of Mandate and/or Prohibition
Exhibit D	Claimant's Lodgement of Race Date for Southern California Racing Meetings 2009 to 2011.
Exhibit E	Claimant's Lodgement of Exhibits 1 through 16, inclusive, in Support of Opening Brief
Exhibit F	Opening Brief (Defendant/Respondent)
Exhibit G	Supplemental Brief (Defendant/Respondent)
Exhibit H	Declarations of John Sturgeon, Michael Kempel, et al in Support of Opening Brief (Defendant/Respondent)
Exhibit I	Response Brief of Claimant San Luis Rey Racing, Inc. Doing Business as the San Luis Rey Downs Training Center
Exhibit J	Notice of Ruling (Defendant/Respondent) dated March 22, 2013
Exhibit K	[Proposed] Findings [Supplemental Brief and Declarations submitted concurrently herewith (Defendant/Respondent)
Exhibit L	Photocopy of B & P Code sections 19607, 19607.1 and 19607.2
Exhibit M	SCOTW Ltd Supplemental Information December 31, 2011 and 2010
Exhibit N	SCOTW Ltd Notes to Financial Statements December 31, 2011 and 2010
Exhibit O	SCOTWINC Articles of Incorporation (i)-(m) Amended 2011
Exhibit P	Southern California Off-Track Wagering, Inc. Off-Site Stabling 2002-2008
Exhibit Q	Transcript of CHRB meeting December 1, 2000
Exhibit R	Minutes SCOTWINC Off-Site Stabling & Vanning Committee, August 26, 2009
Exhibit S	Plaintiff/Claimant's Binder of Exhibits labeled 80-98

Exhibit T	Articles of Incorporation of SCOTWINC
Exhibit U	Bylaws of SCOTWINC
Exhibit V	Shareholders Agreement (March 16, 1988) among SCOTWINC et al
Exhibit W	SCOTW Ltd. Limited Partnership Agreement (March 16, 1988) among SCOTWINC et al
Exhibit X	2009 Spring-Summer Race Agreement (Hollywood and TOC)
Exhibit Y	2009 Fall Race Meet Agreement (Hollywood Park Fall and TOC)
Exhibit Z	2010 Spring-Summer Race Agreement (Hollywood and TOC)
Exhibit AA	2010 Fall Race Meet Agreement (Hollywood Park Fall and TOC)
Exhibit BB	2011 Spring-Summer Race Agreement (Hollywood and TOC)
Exhibit CC	2011 Fall Race Meet Agreement (Hollywood Park Fall and TOC)
Exhibit DD	2009 SCOTWINC to Hollywood Park Checks and Accounting
Exhibit EE	2010 SCOTWINC to Hollywood Park Checks and Accounting
Exhibit FF	2011 SCOTWINC to Hollywood Park Checks and Accounting
Exhibit GG	Closing Administrative Brief of Claimant, San Luis Rey Racing, Inc. (Plaintiff/Claimant)
Exhibit HH	Final Brief (Defendant/Respondent)
Exhibit II	Transcript of Instant Matter, March 25, 2013 (selected pages)

APPLICABLE LAW

Division 8, Chapter 4, California Business and Professions Code section 19433

The board may visit, investigate, and place expert accountants and such other persons as it may deem necessary in the office, track, or other place of business of any licensee for the purpose of satisfying itself that its rules and regulations are strictly complied with.

Division 8, Chapter 4, California Business and Professions Code section 19535

(a) Notwithstanding any other provision of law, at the time the board allocates racing weeks, it shall determine the number of useable stalls that each association or fair shall make available and maintain in order to

conduct the racing meeting. The minimum number of stalls may be at the site of the racing meeting or at board-approved offsite locations.

Division 8, Chapter 4, California Business and Professions Code section 19607

Notwithstanding Sections 19605.8 and 19605.9, when satellite wagering is conducted on thoroughbred races at associations or fairs in the central or southern zones, an amount not to exceed 1.25 percent of the total amount handled by all of those satellite wagering facilities shall be deducted from the funds otherwise allocated for distribution as commissions, purses, and owners' premiums and instead distributed to an organization formed and operated by thoroughbred racing associations, fairs conducting thoroughbred racing, and the organization representing thoroughbred horsemen and horsewomen, with each party having meaningful representation on the board of the organization, to administer, pursuant to the supervision of the board, a fund to provide reimbursement for offsite stabling at board-approved auxiliary training facilities for additional stalls beyond the number of usable stalls the association or fair is required to make available and mantain pursuant to Section 19535, and for the vanning of starters from these additional stalls on racing days for thoroughbred horses.

Division 8, Chapter 4, California Business and Professions Code section 19607.1

. . . . .

(c) The training facilities and amenities provided for offsite stabling and training purposes shall be equivalent in character to those provided during racing meetings of the association.

(d) Upon the request of any party within the organization, the board shall adjudicate any dispute regarding costs, or other matters relating to the furnishing of offsite stabling and vanning. The board may, if necessary, appoint an independent auditor to assist in the resolution of disputes. The auditor shall be reimbursed from the funds of the organization.

(e) The organization may maintain a reserve fund of up to 10 percent of the total estimated annual vanning and stabling costs. In addition to the reserve fund, if the funds generated for offsite stabling and vanning are insufficient to fully reimburse racing associations for expenses incurred during the offsite vanning and stabling program, the organization may accumulate sufficient funds to fully reimburse those associations for those expenses.

(f) The amount initially deducted and distributed to the organization shall be 1.25 percent of the total amount handled by satellite wagering facilities authorized under this article in the central or southern zone on thoroughbred racing, but that allocation may be adjusted by the board, in its discretion. However, the adjusted amount may not exceed 1.25 percent of the total amount handled by satellite

wagering facilities, to pay expenses and maintain the reserve fund for the continuing support of the program.

FINDINGS OF FACT

Findings of fact in this matter are somewhat brief because there is little dispute about the facts (except for the nature of the "organization" under the law) and because the real disagreement involves what the law requires.

I

The CHRB audit report of 2012 was conducted in accordance with the law.

II

All payments from the stabling and vanning fund were made directly from SCOTWINC to the auxiliary training facilities.

III

The nature of the organization as designated by the law to manage and distribute the stabling and vanning fund is somewhat ambiguous. Both SCOTWINC and the Stabling and Vanning Committee both seem to fulfill certain functions.

IV

The Stabling and Vanning fund has been used for purposes other than stabling and vanning.

DISCUSSION

In some ways, the two issues that are required to be examined are simple. Unfortunately, for the CHRB to fully understand and advocate a position in the underlying civil suit, the two issues cannot end the inquiry. That is, there was ample evidence that the CHRB auditors completed a thorough and exhaustive inquiry into whether the payments that SCOTWINC made for reimbursement were actually paid in accordance with the association's license application at the approved rate. To that extent, one could assume that the stabling and vanning funds were properly allocated but that would only be a superficial conclusion and would not address the underlying disagreement in this matter – what the law requires and how it should be interpreted. SLRD has made multiple accusations with respect to how the law has been applied, some of which have merit, while others do not. It is not the aim of this proposed decision to resolve the civil matter under the law but rather to explain and determine what the law requires. Interestingly, it is clear that the law has, at best been misinterpreted, and at worst but violated, but even given these problems, it is unclear whether SLRD would have benefitted had the law been applied properly. However, determining whether SLRD has suffered some damage is beyond the scope of this inquiry.

In 1990, the California Legislature amended and finalized a law at the behest of the racing industry in order to deal with the issue of a horse population too large for a single track and to compensate fairly horsemen who are obligated to stable away from the racing site and van to the racing site for the races themselves. The law sets aside up to 1.25% of the satellite wagering handle in order to pay for the incremental costs associated with stabling horses at a facility apart from the track running at the time and to pay for the vanning of those horses to the association in order to race. The CHRB was placed in charge of managing the exact percentage of handle and the law set up an organization that would be manage the fund itself--disbursing the funds to the appropriate associations in accordance with the provisions of the law.

As an initial matter, there was some concern on both sides of the matter with respect to who exactly the parties were and more to the point what entity or entities owned SLRD and the associations. Apparently, all of the associations were named as Respondents in the original lawsuit as well as the CHRB itself. Since then, most of the parties have since been excused except principally Hollywood Park. Some of the parties were obviously removed from political reasons and others were removed for strategic ones. However, it is clear that the CHRB and the associations have all interpreted or failed to interpret the law in the same way, so the application of this and future interactions should not be limited to Hollywood Park. Furthermore, for purposes of this inquiry and for purposes of determining what the law says, the actual corporate entity that owns the particular association or offsite training facility is inconsequential. To wit, the claim that any money intended to be paid to Hollywood Park as a racing association that was paid to the corporate entity that owns Hollywood Park is of no consequence under the law.

Fortunately, the legislature passed a law that is clear and does not have to rest on intent or statutory interpretation but rather on plain meaning. Quite simply, if an association conducting a live racing meet determines that it requires stalls beyond which it can itself provide "in order to conduct the racing meeting" that it seek reimbursement for the incremental costs of maintenance and availability of those additional stalls secured at a Board-approved auxiliary training facility. The law requires that it seek that reimbursement from an organization whose structure is explained in the law and the whole framework is to be overseen by the CHRB. Unfortunately, the straightforward nature of this arrangement has proven difficult to follow for most of the parties involved.

To a large extent, the CHRB has ignored its responsibility to oversee the application of the law mostly through inaction and in two instances, actual affirmative action in contravention of the law. Typically this entire process begins when the racing association applies to the CHRB for approval of racing dates. On the application, the racing association is required to list the number of stalls it can provide for the meeting as well as the number of additional stalls required to conduct its race meeting. There appears to be little scrutiny when it comes to this portion of the application. For example, in 2011, Fairplex Park applied to conduct a three week racing meet. In its application, it listed 1346 as the number of stalls it could provide and then listed 1000 as the total number of additional stalls that it wished to provide on offsite locations. *See Exhibit S.* While the law allows for

reimbursement of money used to provide enough stalls "in order to conduct a racing meeting" and it is clear that associations should be given great latitude in determining what that number should be, no one can reasonably argue that 2346 stalls were necessary for a three week meeting. Furthermore, Fairplex wished to allocate those additional stalls in the following way: Hollywood Park 300, SLRD 200 and Santa Anita 500. Surely, even a cursory examination of this application would have concluded that Fairplex should not be reimbursed for such a fiscally irresponsible arrangement. Additionally, the application asks to be provided with the agreement between the association and the entity furnishing the offsite stabling. The response on all applications is "on file." Putting the failure to provide the pertinent agreement aside, further inquiry would indicate that the "on file" agreement is not between the track and the auxiliary facility as the law requires, but between the organization (SCOTWINC in this case) that manages the stabling fund and the off track facility providing additional stabling. Finally, in a particularly troubling use of the stabling funds, in 2008, the CHRB approved a plan to disburse almost $600,000 of the Stabling and Vanning fund to Fairplex Park for capital improvements to the barn area and tacitly approved the Stabling and Vanning Committee's decision to use the fund to provide money to an organization providing medical services to backstretch workers. While perhaps important, both uses of Stabling and Vanning funds for these purposes were in direct contravention of the law. To its credit, a subsequent audit performed by the CHRB itself concluded that this money was an inappropriately disbursed and required its return.

One of SLRD's main objections to the manner in which these laws have been implemented is the nature of the organization responsible for distributing the money in the Stabling and Vanning fund itself. The law requires that there be "an organization formed and operated by thoroughbred racing associations, fairs conducting thoroughbred racing, and the organization representing thoroughbred horsemen and horsewomen, with each party having meaningful representation on the board of the organization." The organization that receives the money from the satellite wagering handle, holds the money in bank accounts and distributes this money by check or wire transfer is SCOTWINC, which all parties agree cannot be considered the "organization" contemplated by the law because it includes parties beyond the ones listed such as quarter horse associations and other groups. Respondents contend that the group that administers the Stabling and Vanning fund is a separate entity within SCOTWINC known as the Stabling and Vanning Committee. Frankly there is ample evidence to support both contentions. While there are occasionally minutes from the Committee itself, it has some bylaws, and the commissioners at CHRB meetings occasionally refer to this Committee as a separate entity, there is some degree of legitimate confusion. Industry leaders refer to SCOTWINC and the Stabling and Vanning Committee interchangeably and the CHRB's official position is that it recognizes SCOTWINC as the organization which administer the Stabling and Vanning Fund. *See Exhibit S-86.* To reiterate, the evidence is frankly ambiguous. It makes sense that SCOTWINC retain and distribute the money from an efficiency standpoint but in order to fully comply with the law, there must be a clear, distinct entity with real members and regular meetings that actually administers the fund.

Next, the issue of reimbursement is particularly troubling. The law requires that the fund be used to "provide reimbursement for offsite stabling at board-approved auxiliary training facilities." The plain meaning of the law is that the association determines how many additional stalls it requires to conduct a race meeting, the association negotiates a contract with an auxiliary training facility to provide the additional stalls it requires, pays that auxiliary facility and then seeks reimbursement from the organization administering the fund. The word "reimbursement" has only one meaning and it is not what is currently taking place. At present, SCOTWINC writes a check directly to the auxiliary training facility. The law requires that the funds be distributed to associations themselves and this current scheme cannot be construed as reimbursement. Respondents argue that it is simply more efficient this way, that the contracts are between the organization and the auxiliary facility and that the associations would suffer a financial burden if they had to pay auxiliary facilities and then wait for reimbursement. While all of these may be true, they do not comport with the requirements of the law. The law was established to create a structure in which the associations would have incentives to be frugal and efficient in determining how many additional stalls it required and negotiate the best rate it could. The law further provided oversight by the organization and by the CHRB itself. At present, there appears to be no safeguards against using the fund in an economically inefficient manner and in fact most evidence indicates that it almost a goal to try to figure out how to use the entire 1.25% rather than require some efficiency. While the economics of racing are not presently overly favorable to associations, ignoring the law cannot be permitted. If the current legal framework is untenable, the law should be changed or the associations can easily comply with it by negotiating contracts with the auxiliary training facilities that require monthly payments or even shorter periods in order to minimize the outlay of large sums of money while waiting for reimbursement.

Finally, some other issues should be noted as well. The import of this law is less significant than it was when it was originally written. To wit, the horse population has steadily decreased over time, requiring fewer additional stalls. Given that the law allows associations wide latitude in determining the number of stalls necessary to conduct a race meeting (with oversight by the CHRB), complying with its provisions is not particularly difficult, especially today. Nevertheless, the provisions still exist and must still be followed. Next, the manner in which rates are determined for providing additional stalls is somewhat troubling. There appears to be a general acceptance of having to pay whatever the auxiliary facility requires, rather than any real determination of actual incremental costs or negotiation of rates. This is partly true because associations realize that they also will act as auxiliary facilities at some point during the racing calendar and therefore are happy to overpay because they know that they will be overpaid in return. In a very real way, this is why a facility that only serves as an auxiliary training facility such as SLRD finds itself in the position it does – it can never receive the reimbursements under the law because it does not provide racing. This is why actual oversight by the organization and the CHRB is critical. In particular, there must be some determination about the efficacy of associations paying offsite facilities a flat fee to keep the whole facility open, rather than for a specific number of stalls. In the end,

this may be the most economically efficient framework, but there should be actual evidence behind it and certainly in this day and age when less additional stalls are necessary. Lastly, while it is beyond the scope of this hearing, it is unclear that even if the law had been properly applied since its inception, to what extent San Luis Rey Downs may have benefitted, or more to the point suffered some detriment. It should be noted that despite the foregoing, the decisions with respect to reimbursement cannot be purely driven by economics – that considerations such a goodwill with horsemen, service to the industry and minimizing disruption in stabling are legitimate factors that can be considered while still respecting the legal framework created in an environment with limited resources.

CONCLUSION

While this is not a traditional proposed decision in the sense that a recommendation is made to the Board as to which party should prevail, given the issues at hand there are some recommendations that seem appropriate: (1) The Audit Report dated November 6, 2012, performed by the Audit Unit of the CHRB, is in accordance with the law; (2) the Stabling and Vanning funds have not been properly allocated in that they were distributed as payments to auxiliary training facilities rather than reimbursements to the associations; (3) the CHRB must take a more active role in scrutinizing license applications of associations with respect to stabling; (4) the Stabling and Vanning fund should only be used for stabling and vanning; (5) agreements with regard to additional stabling should be between the association and the auxiliary training facility; (6) the organization or Stabling and Vanning Committee should be more independent from SCOTWINC; and (7) reimbursements from the Stabling and Vanning Fund should be made to the associations for the costs associated with the additional stalls.

DATED: July 5, 2013.

C. SCOTT CHANEY
Referee