



Establishing a Breed to Race Incentive

Introduction

The purpose of this paper is to outline a proposed Breed to Race incentive designed to significantly increase current levels of racehorse participation.

The thoroughbred wastage study completed earlier this year identified that from a foal crop of 4,000 live foals:

- approximately 980 foals will never be registered with a trainer;
- 61% (600) of these horses will be fillies and 39% (380) will be colts.

We are not aware of any genetic or physical reason why fillies might be markedly less capable of racing and conclude that a large number of fillies from each crop do not race for economic or commercial reasons. A filly with a lesser pedigree may not be raced given the current cost/return equation, the lack of a secondary market (and therefore an exit opportunity as exists for colts regardless of pedigree) and, absent achieving black type, the minimal residual value as a broodmare.

If one (conservatively) assumes that all 380 colts in this segment are not registered with a trainer due to physical inadequacies and a similar number of fillies have the same physical issues, this would suggest that at least 220 fillies per crop are capable of racing but are denied the opportunity to do so.

Based on the average racing career of 2.5 years calculated in the study, this would suggest that at any time approximately 550 fillies exist within the supply chain that could be activated as racing participants - if there was adequate financial incentive. Based on current annual starts per starter ratios of 5.6, this represents a potential 3,000 starts per annum, being approximately 10% of current annual starts.



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In addition to attempting to activate these untried fillies, the Breed to Race incentive discussed herein could also increase total annual starters and starts via a combination of:

- Generating a greater number of starts from existing active horses within the supply chain, including approximately 300 fillies per crop that are currently retired sound following a relatively small number of starts due to a lack of ability and/or a perceived lack of opportunity.
- Increasing the number of foals being bred as this proposal will expand the range of commercial options and outcomes available to a breeder if a filly is produced.

A Breed to Race incentive would recognize the key role breeder/owners play in the supply chain – arguably a greater role than any other individual participant. Bonus payments would only go to those parties “doing the heavy lifting” and would not be paid to breeders that sell their horses – other than to the extent they also retain and race other horses in New Zealand. This initiative therefore targets a segment of breeders that is currently in decline and can be pitched at a level that has the potential to impact their propensity to race a filly and their breeding decision.

Importantly, this initiative is not an incentive scheme designed to increase production without addressing the issue of demand. Rather, it attempts to stimulate demand which initially can be satisfied from existing unutilised production and - over time - may lead to an increase in production.

If necessary, it would be possible to validate the magnitude of the pool of horses being targeted by undertaking a sample survey (probably by phone) of the owners of horses in the segment “never registered with a trainer” for a selected crop – say 2002 (now 6yo). This survey could establish the factual reason why horses in this segment did not progress through the supply chain. It may also be possible to test whether horses might have been activated if a Breed to Race incentive had been available however, responses to such questions would be speculative.

The Proposal

A Breed to Race incentive is established where bonus payments are offered to the breeder of the winner of a specified number of races each year, distributed throughout the racing calendar.

To be eligible to receive **part or all** of any bonus, two criteria must be met:

- The registered breeder must also be a registered owner of the winning horse;
- The winning horse must be a filly or mare, three years old or older;

The proportion of the bonus that is paid to the breeder is determined by the **lowest** percentage of owner/breeder commonality. For example:

- If a 100% registered breeder of the horse retains a 100% registered ownership when the horse is raced, then 100% of the bonus would be paid.
- If a 100% registered breeder of the horse retains a 50% registered ownership when the horse is raced, then 50% of the bonus would be paid.
- If a horse is bred 50/50 by two breeders who each retain a 10% registered ownership when the horse is raced, then 10% of the bonus would be paid to each of these breeders – i.e. 20% of the bonus would be paid.
- If a horse is bred 50/50 by two breeders but is raced 100% by one of these breeders, then 50% of the bonus would be paid to the breeder that retained ownership of the horse.
- If a horse is sold or leased by its breeder and raced by third parties, no bonus would be paid.

The size of the scheme (number of bonuses offered and the value of the bonus) would need to be explored with NZTR based upon projected cost/benefits however the scheme would need to be of sufficient scale to provide a tangible incentive for a breeder who has bred a filly, to put that filly into work.

This paper assumes that 200 bonuses of \$15,000 are offered nationally, representing a nominal scheme size of \$3 million per annum - albeit actual bonuses paid would in all probability be substantially lower. While some bonuses may be offered on races restricted to fillies and mares, most would attach to races open to colts and geldings, effectively reducing the probability of the bonus being struck.

It is proposed that bonuses would not be attached to black type and/or iconic races that already offer significant stakes.

A decision would need to be made whether the \$15,000 bonus is paid only to the winners of specified races or whether it would be shared across the first three place-getters. The data (below) suggests the economic cost of either scenario would be similar. This decision should therefore be driven by which scenario is likely to have the biggest positive impact on participation. It is believed offering the total bonus to the winner would be more effective.

Similarly, it is believed all of the bonus should be paid to the owner - without trainer or jockey percentage deductions. Trainers and jockeys will directly benefit from the scheme via an increase in horses in work and total annual starts.

As the fillies being targeted have already been bred and are immediately available, it is possible that the lead time between initiating the scheme and achieving a positive impact could be relatively small. This contrasts with production based schemes that have 2-3 year lead times requiring substantial investment prior to validation.

Notwithstanding this, if there was a desire to implement the scheme progressively, it could initially be introduced into 3yo races in the first season, 3&4yo races in the second season and so on.

Estimated Cost of the Scheme

- In the 2007/08 racing season there were 5,576 individual horses that started in at least one race.
- Of these, 2,507 (45%) were raced by one or more owners that were also recorded as a breeder of the horse – i.e. the breeder had retained an ownership interest in the horse.
- In some instances there was 100% owner/breeder commonality but in many instances the commonality percentage was less than 100%.
- Retrospective calculations are made difficult by the fact that ownership changes occur during the year, impacting commonality percentages – both up and down. Data on breeder percentages has also not always been complete requiring some assumptions to be made in this analysis.
- We estimate that average owner/breeder commonality of the 2,507 horses equated to between 1,600 – 1,950 horses – i.e. these breeders on average had retained 64% - 78% ownership of the horses they had bred.
- Accordingly, on a weighted average basis, owner/breeders represent 29% - 35% of all owners.
- Of the 2,507 horses with some owner/breeder commonality, 1,742 earned stake money and 765 earned none.
- Of these 2,507 horses, 825 horses won 1,220 races earning total stakes of \$14.375m.
- The owner/breeder weighted average percentage equated to 850 races (70%) and \$10.192m (71%).
- This represents 29% of the 2,970 races run.
- 28% of all stake money was won by owner/breeders on a weighted average basis.
- From the wastage study data derived from past crops, we know that for each crop, after allowing for the impact of exports (majority colts); approximately 54% of the total horses raced are fillies and 46% colts. In contrast, 48% of winners are fillies and 52% colts and 43% of the races won are by fillies and 57% by colts. The export of colts cause the population to have a filly bias however as the remaining colts race longer and more often, fillies are currently under-represented in winners and wins.

- While the introduction of the proposed Breed to Race bonus may cause the percentage of races won by fillies to increase and trend towards 50%, it is unlikely that materially more than 50% of the races will be won by fillies. This trend can be monitored and responded to in the unlikely event the scheme caused a significant distortion.

Assuming 200 x \$15,000 bonuses were offered, the estimated annual cost would be:

Cost = 200 x \$15,000 x 29% x 50% = \$435,000 per annum.

Industry Breakeven = \$435,000 ÷ \$25,000 = 17.4 additional starters per crop.

Thoroughbred Code Breakeven = 17.5 ÷ 56% = 31 additional starters per crop.

Accordingly, for this initiative to breakeven from an NZTR perspective, it would require 14% of the estimated pool of 220 available fillies per crop to enter the racing population and participate at or above the average.

This breakeven would reduce if the participation of fillies in other segments within the supply chain also increased as a result of the introduction of the scheme – which is likely.

This indicates a high probability the benefits to both the thoroughbred code and the industry will exceed the costs – suggesting the proposal would be “self funding”. If notwithstanding this, NZTR’s willingness to support this proposal became dependant on a portion of the scheme’s cost being sourced from within the breeding industry; NZTBA would be prepared to approach studs to seek such support.

Breeder – Owner Commonality

It is envisaged the commonality calculation would be similar to the taxation continuity rules and the **lowest** commonality percentage would be applied to bonuses. If the highest commonality percentage was applied, the scheme would cost significantly more and could be open to manipulation to increase the eligibility of horses for bonuses.

A complicating factor is that horses may be bred and/or owned by a range of entities including individuals, partnerships, syndicates, trusts, estates or companies.

If the scheme was required to trace the effective percentage ownership of an individual through these different entities, administration of the scheme would quickly become complex and there would be instances where qualifying bonus payments would not be identified. The shareholding of companies and the beneficiaries of trusts are also not a constant.

We believe a number of “rules” should be established to simplify the eligibility for bonuses and the administration of the scheme:

- To qualify for a bonus, a minimum commonality percentage of say 15% would be required.
- Commonality would only be recognized at the first level – i.e. if the registered breeder or the registered owner was (or included) a company, no attempt would be made to ascribe an effective interest to that company’s shareholders. To qualify for the bonus, the company would have to race the horse that it bred. Similarly, no attempt would be made to “look into” the membership of registered syndicates or the beneficiaries of trusts.
- Further constraints may need to be placed on the eligibility of companies or trusts to counter changes in shareholding or beneficiaries.
- As the registered owners of a horses raced by a partnership are the individual partners, it should be possible to treat partners in the same way as individual owners who jointly race a horse.

NZTR’s ownership database precisely records the percentage ownership of a horse being raced however its breeding database is currently less precise. While the breeders of each horse are recorded, the percentage each breeder represents of the whole is not always recorded. There may therefore be some difficulty performing commonality calculations in a number of situations.

It will be possible to establish “rules” that will initially operate to establish the “default” breeder percentage in such situations. (For example – in the absence of existing information to the contrary, the default breeder percentage could reflect the ownership percentages of the dam.) In the future, the breeder percentage could become information NZTR captures accurately for every horse at the time of initial registration, just as ownership percentages are currently captured.

Other Potential Issues

1. The risk that a higher than projected percentage of bonuses are struck.

Like other schemes in the past, the “offering” would need to be worded so as to provide sufficient flexibility to manage the number of bonuses offered in order to mitigate this risk, if required. Another option might be to cap the number of bonuses that can be won by a horse in a season.

2. NZTR was previously engaged in a protracted dispute over the TBS scheme with the owner of a competing bonus scheme.

A Breed to Race incentive open to a subset of fillies without the need to register or make a nomination payment is very different to the existing bonus scheme. Examples of similar incentives already exist on a small scale (e.g. The Dunstan Stayers winner’s bonus). Care should nevertheless be taken to ensure this initiative does not reactivate past litigation.

3. The risk of breeder and/or ownership registrations being manipulated to increase the eligibility of horses for the incentive.

The scheme would be reliant on the rules of racing that prohibit a horse being raced with an undeclared ownership interest. The working group proposed below will need to explore whether opportunities exist and how these can best be countered.

Recommendation

We recommend:

1. NZTR includes a Breed to Race incentive in the short list of participation initiatives currently being researched.
2. A working group is established to consider this initiative in more detail. NZTBA would welcome the opportunity to participate in this working group and help develop this initiative further.

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