



Race Track Industry Program

THURSDAY, DECEMBER 8, 2005

WAGERING SYSTEM POLICING

Moderator:

Ed Martin, President and CEO; Association of Racing Commissioners International

Speakers:

Charles Champion, President, CEO, Chairman; Youbet.com, Inc.

Craig Fravel, President; Del mar Thoroughbred Club

Cheryl Ritchko-Buley, Board Member; New York Racing and Wagering Board

MR. DOUG REED: We have one brief presentation before this panel gets started. I would like Wendy Davis to come up here and make a presentation on the award that we had to postpone until now.

MS. WENDY DAVIS: Thank you, Doug. Better late than never as they say. Our award winner was busy at another conference, but he's here now.

What we would like to present this morning is the John K. Goodman Alumni Award, and this is awarded every year to one of our outstanding graduates who are out in the industry making a difference.

And this year's winner is Dr. Scot Waterman. I think many of you know Scot. One of the things that we were so proud of is Scot seems to be everywhere. If there's a conference, he's out educating people about what he does, and I always get this wrong, I always think that you're one of those Canadian mounted police guys. The RMTC, the Racing Medication Testing Consortium. He's the executive director and does tremendous work.

He really works tirelessly to do some things that this industry said could never be done, and that's working towards uniform medication rules; and although we're not there yet, I think we're now in the same book getting to the same page.

And, Scot, when he came to the Race Track Industry Program, already had his DVM, he had a small animal practice and dealt with cats and dogs, and I know he's kind of a cat kind of a guy so I guess that's why he's doing so well, because trying to get these rules together is like herding cats.

So, Scot, you're doing a terrific job. Everyone in the industry really appreciates it and we are so very, very proud of you as a graduate of the Race Track Industry Program.

If you would like to come up, we have a little something for you.

(Applause)

DR. SCOT WATERMAN: I'm sure most of you didn't come here this morning to hear a speech from me so I'll keep this mercifully brief, but I certainly would be remiss if I didn't thank a few people.

I'm the only paid employee of the Consortium, which means that all of the members of the board of directors are volunteers. They give freely of their time.

When I call a meeting they are there so certainly they are the ones that should share in this award as much as I.

Second, I would like to thank the regulatory community. Couldn't be more appropriate considering the panel this morning. Without their guidance and support of what we're trying to do, I can certainly tell you I wouldn't be standing here today.

And lastly, just want to thank the Race Track Program. The year and a half here that I was here was tremendous. Wendy, Doug, John Walzak, at the time. I've gotten to know Steve through the Model Rules process. They certainly create a wonderful environment here in Tucson to learn about this industry. So I strongly encourage anybody that's considering sending anybody here to do so.

So now back to your regularly scheduled programming. Thanks.

(Applause)

MR. REED: Thank you, Scot.

I would like to introduce our moderator and get started today for the final day. We've got a full schedule again as usual.

Ed Martin was former director of the New York Racing and Wagering Board. He was co-chair on New York Medication Advisory Council. He has served on the Commission on Casino Gambling in New York. He was senior aide and strategist for the majority leader of the New York State Senate.

He worked in D.C. for the Federal Energy and Regulatory Commission, so certainly someone very familiar with the regulatory environment.

Please welcome the president and CEO of the ARCI, Ed Martin.

(Applause)

MR. ED MARTIN: Thank you, Doug. Thank you all for getting up and being here this morning.

As they were describing the wonderful work of Scot Waterman all I was thinking of was the Woody Allen movie Zelig, of how Scot Waterman is kind of the Zelig of racing, popping up all over the country at conferences and racing commissions pushing for uniformity in medication rules.

You're pretty close to getting that, Scot, and we could probably start using you on the wagering and security issue.

How many of you in this room have ever heard the name Erin O'Donovan? Nobody. Erin O'Donovan was/is an investigator in the licensing division of the New York State Racing and Wagering Board. And she was marshalled to the task in 2002 when the Breeders' Cup Pick-6 debacle hit this entire industry, along with other people on our board at that time, to figure out what happened, who did it, how they did it, and then to unmask the evidence necessary to hand off to the U.S. Attorney in New York and result in a successful prosecution of Chris Harn, Glen DaSilva and Derrick Davis.

The reason why I bring Erin O'Donovan's name forward to you is because Erin O'Donovan is one of those faceless people who none of you know and none of you will ever see. She's never invited to one of these conferences, she's never written about in any of the press, she never gets an award, but Erin O'Donovan was the investigator who found the link that these three individuals lived together in a frat house at one point in their career.

Erin O'Donovan was very important to the entire effort to build that case, and that case was built pretty quickly when you consider that it was only about two weeks from the point when the crime was perpetrated and, thank heaven, Volponi won the race, but what that did, that woke all of us up to the fact that all of us in the industry, the regulatory commissions, had a new issue we needed to deal with.

It was an issue probably we collectively should have been dealing with. You know, it's funny that you come to conferences like this and there's so much time and effort put on the medication issues. You know, the drug positives, all the tests that are taken on the horses in this country and all the effort that goes into that and all the expense and so forth, and it's pretty much only one percent come out positive, and we know that. We can measure that. That's quantifiable.

Today, we stand here today and we have issues that have not fully been addressed since the Breeders' Cup incident, and there's been a lot of discussion and great people who have come to the cause and the task to solve a problem for this industry.

There's been a lot of effort, a lot of committees, a lot of ideas, and at the end of the day we still haven't created what everybody uniformly agrees is needed, and that is a national wagering monitoring system and a national wagering security database.

Last year RCI, which I'm honored to be serving as their president, and I'm also honored, by the way, to be serving all of our new jurisdictions who just merged with NAPRA so everybody who wants one stop shopping for your regulators, you've got it with Paul Bowlinger and I at the RCI offices, and thanks to all of you that worked on that process.

(Applause)

Last year RCI passed a resolution. There was a lot of talk in the NTRA about by creating a National Office of Wagering and Security, and the regulators across the country were getting a little antsy that nothing was happening and the industry wanted to do it and everybody was trying to be supportive of that.

And RCI passed a resolution, gave a couple months deadline as to, we want to see the plan. We want to know when you're going to launch it. We want to know when it's going to happen. And the deadline came and went and nothing happened.

So regulators get together and say, "What are we going to do?" We can't shut everything down. What would that do to all the people who depend on this great industry. So we started getting involved with an effort at the NTRA. We were graciously invited to be participants on a steering committee to study the feasibility of creating — well, it kind of morphed from an Office of Wagering and Security, National Office of Wagering and Security, into a National Office of Racing Integrity.

The entity hadn't exactly gotten off the ground and it was already expanding. And everybody was saying we want the regulators involved, we like to have a situation where the regulators can play a pivotal role. We certainly want to partner with the industry.

We've had a really great dialogue over the past several months trying to get to that point. But we still haven't reached a consensus between the various associations that represent the industry and now the one association that represents the regulators of the industry.

So we felt that if this was — we could continue to work with everybody and we would like to do that, but somebody has got to jump-start this process and get this going. We have been talking about it, the technology is there, the expertise is there, so what we did is we went out and we found two great willing partners in ESI Integrity and Izzy Sokowski.

These, ESI and Izzy are not strangers to the issue of wagering and security in this industry and we said, "Hey, would you — we want to get this going.

And we've developed a business model and a business plan that was unanimously endorsed by RCI's Wagering Systems Security Committee and yesterday was unanimously endorsed and authorized by the board of directors of RCI in a meeting with all of our new affiliated members that just came over from NAPRA, and it was unanimous.

So you will probably see in the trades today that there's a new company coming on the scene called RCI Integrity Services, and what that is they are basically going to provide is wagering, monitoring and integrity services, create a national database, and obviously a lot of people were saying you're not going to get any customers. What are you going to do if you don't get any customers.

I said, well, I think that the need, the demand for this service, this product which is going to be handled through a not-for-profit corporation, therefore, RCI doesn't have a profit motive, obviously the technology people have to get paid, they wouldn't get paid under any configuration, so we'll do this at cost.

We said, well, we're going to have customers, and so we started talking to people and one of the first guys we talked to, because we had heard that they were in the process of developing something that was going to serve their needs, was Chuck Champion.

And I have to say, Chuck, a couple of years ago nobody here knew who you were and now all of a sudden everybody knows who you are.

MR. CHARLES CHAMPION: Somehow he thinks that's an advantage.

(Laughter)

MR. MARTIN: And what I've noticed since I first met Chuck is the bigger his company is getting, the slimmer he gets.

(Laughter)

So Youbet, and this was before we even knew about the United Tote, Youbet said what you're doing is the right thing. I don't want to speak for you, Chuck, but they said we want to be a customer.

We said, wow, so we put some numbers on a business plan and figured out, okay, who is the second customer going to be. And then there were discussions with Scientific Games and next thing Scientific Games said, "You know, we like this, we want to be your customer."

I've got to be honest with you folks, we just got this thing authorized yesterday and before we took it to the RCI board already we've got over 50 percent of the U.S. racing handle going to now feed into this RCI Integrity Services and database which our business plan calls for commencing operations in the second quarter of 2006.

And we would hope, we really hope that if this industry is serious about everything it has said it has wanted for the past several years of doing what all of the experts have said needs to be done, here it is. We're asking everybody to buy into it. And we hope you can support it.

Now, we realize that there may be potential competitors down the road and we feel the expertise between ESI and the technology from Izzy Sobkowski's company will provide a product second to none.

And I'm not a technical person. I sat with Greg Avioli and we were talking technical stuff, and I said, "Listen, Greg, if you're going to ask me the technical questions, you've got to ask Alan Ahac or Izzy. I can't answer those questions. I know what I know and I know what I don't know."

But I do know this, the time is now and we invite everyone — by the way, there are model rules being discussed, being proposed, but in some states are actually being promulgated like in New York that are going to require wagering system operators to employ the services of an independent monitor.

It's kind of odd to require somebody to employ the services of something that doesn't exist, so we had got a real practical issue and that is, before anybody can require it, we've got to make sure it exists, and that's what we're doing. And we're not in competition with anybody. We're not trying to break away from a cooperative effort on behalf of this industry, but somebody had to step up and start doing it and at the end of the day I don't know any state that's eliminating its racing commission.

We're here, companies come and go, merge, grow, but we're here and our responsibility is to the general public, to the taxpayers and to our constituents and our constituents, are everybody in the racing industry, and we feel we're going to try to do something good for you that everybody has agreed needs to be done.

And with that I would like to now introduce our wonderful panel. We'll go one by one. We didn't draw lots as who is going to get to speak first, but I think we'll start with Chuck Champion, only because he's closest.

So, Chuck is — we all know who Chuck is, we know who Youbet is and we all kind of know what you have been up to.

MR. CHAMPION: Thank you, Ed. First of all, I apologize for a little bit of hoarseness in my voice, and if I'm a little bit slow this morning, it's frankly not because I was out drinking, carousing into the late hours last night, but I did have just real quickly a personal episode where at four in the morning I found myself in my room being startled awake by a six-foot-four security guard of the hotel.

Apparently in his rounds last night he was traveling through the halls and heard some noise coming from my room, and since I didn't answer the door he thought it

would be well if he came inside and checked it out, and I found myself startled awake by this guy.

He said it took him two or three minutes to shake me out of what was apparently a bad dream, and I kept saying over and over again, "Oh, my God, Lorne, what have I done, what have I done? I did what?"

By the time — by the time I calmed down, one thing or another and the security guard said, "It must have been a horrible dream. What the hell did you do?" And I said, "Well, all I remember is that I basically took everything I had, entered into an agreement, everything I earned and I put it in this agreement, I was going to go out and sell most everything I had and borrow a hell a lot of money, more than I ever had to get this thing done and all my friends that knew a little bit about me and knew about Ed sat there and said, 'you know, it probably isn't going to work out and you're really going to be sorry', and it scared the hell out of me."

He said, the guard said, That would scare me, too." And he said, By the way, who is the hell is Lorne? I said, oh, Lorne, that's my divorce attorney."

(Laughter)

I told this story not only because I enjoy kidding Lorne but there were a number of things in that story that were absolutely true and there are other things in that story that are absolutely, as you well know, absolutely not true, and I use certain facts to my advantage to take you to a place that I wanted you to go.

In this case I wanted to take you to a place where I could try to amuse you a little bit this morning. I did wake up at four o'clock this morning, I was staring at the ceiling, but obviously there was not a six-foot-four guy standing over my bed, and I wasn't writhing in pain and screaming, "Oh, my God, oh, my God, what have I done?"

The fact of the matter is I did have to give up everything in my life and borrow a hell of a lot of money, but my divorce attorney's name wasn't Lorne.

(Laughter)

The point I'm trying to make is that as I make some additional remarks here this morning I'd appreciate the things that are important to you, you write them down on a piece of paper and you don't trust a word that I have to say this morning, not a word, don't take me at my word, don't believe me. Independently check and verify what I have to say as being truthful and accurate, because that is the only way we're really going to keep a deal straight.

The reason I know that is that I spent 35 years in the newspaper industry and for the most part it's unregulated. We all know that. They think they are above law in most everything they do. They do have a culture inside the newspapers that basically state, since we point to everybody else and we accuse them of

wrongdoing, we cannot afford ourselves to be involved in any wrongdoing. If we don't regulate ourselves, we in fact will be regulated, so we work very hard, from the time I was a very young kid in that industry to make sure that we did the right thing before someone else told us what we needed to do was right.

There's a lot of people that I met in this room over the last three years, and I've got some great relationships in the room, and frankly, I probably angered a few of you. For those of you I have, I apologize, because in the early stages of my relationship in this industry, I was trying to save a company that was dying.

Sometimes the drowning man doesn't always recognize who is trying to help you and who is not, sometimes tries to pull you down in the process. So a lot of you can sit there and say I have been brash and sometimes rude and even aggressive and even at other times you can say that I have been naive and don't know anything about the industry, and I sit here today, I can honestly tell you there's still more I need to learn about it than I'll ever have learned in the last three years.

I don't think that any one of you, though, can say that I haven't kept a promise that I've made or looked you straight in the face and haven't told you the truth.

But that's not really the most important thing here today. I think the most important thing for, I hope, everybody in this room to take away from is there is no more important asset that all of us collectively use that are involved with and this is not my line, this is Nick Nicholson's line, and that is the pari-mutuel pool itself is the greatest asset that we have.

We need to protect it at all cost because if our customer bases lose confidence in it, we have lost this industry, we have lost the economic engine that pays all of our bills and all of the bills of the people in this industry.

It is at risk today. We have thousands of people entering in our pools that we do not know who they are. We don't know who owns the companies that run these guest sites. We don't know what compliance standards they use, and we have to. And someone has to step forward, and a number of us are, and that's the reason Youbet is doing this is to allow others to look into our business to know who we are, how we're organized, how we're owned, how we're operated, okay, and have full and total transparency into that.

We're fortunate. We're a public company. We operate under Sarbanes-Oxley and 404, and that means if I do anything as a public officer that's illegal, I'm going to go to a place that I'm scared to death to go, and that is called prison. I know why I need to be frightened of my ex-wife. I definitely know why I need to be frightened of prison. I want to deal with neither one.

(Laughter)

God, I wish she was in the audience.

(Laughter)

And so the point I make is is that I have an advantage because I'm a public company, of course, you know who I am, you know who owns me and you know everything about it. We're also licensed in a number of jurisdictions within the United States; Oregon being one, California being another, Idaho and several others. So we're regulated.

And we've taken the step of anything that we buy to make sure that it's regulated as well. And that's the reason for taking IRG to Oregon and licensing it, so that everybody can understand what we're doing, how we're doing it, why we're doing it and that there's an independent body that reviews it.

The other thing that we feel very, very strongly about is not just transparency, who we are, but it's also compliance that everything that we say in the operating plan is in fact being done the way the operating plan was written and that you expect us, particularly the regulators in this room, to perform.

We file those both in California and in Oregon, and what we've done is we've gone out and we've hired a compliance committee.

The chairman of the compliance committee is a gentleman by the name of Gregg Schatzman. Gregg Schatzman is the chief or was the chief of investigations for the Nevada Gaming Commission. Most of you know Nevada is probably the toughest regulatory environment to get a license in, and it was Gregg's job to make sure that people were licensed there.

In fact, we're not in any way, shape or form nefarious. Gregg found us a gentleman by the name of Steve Rybar who is a former special agent of the FBI who worked in organized crime in Nevada. Also happened to work on some very serious cases cleaning out Asian organized crime in Nevada.

He found a guy named Ron Williams, U.S. Secret Service special agent in charge of credit card theft or identity theft and credit card fraud. We also have guys like Roger Licht, the former chairman of the California Horse Racing Board and Ed Hannah, the former general counsel of MEC. Gordon Dickien, who is the compliance officer with Shuffle Master Gaming Company in Las Vegas, and we basically augmented a team of people that we needed that could bring law enforcement around credit card theft and fraud, organized crime.

We then, once we bought IRG, so everyone knows, we ran their database of customers through 48 separate criminal lists or targeted lists that the United States and Interpol can provide to us to make sure that the customers that were coming into the pool also were clean.

I really am encouraged to say that the customer base at IRG and I'm sure a good number of others contained individuals that are people that we would want to have in the pools that all these people pass screens like cybercrimes, terrorists lists,

money laundering lists, gaming exclusion lists, bank fraud; those things that would be direct threats to the pari-mutuel pool.

And all the customers had to pass those tests or we wouldn't take the bets, so we know who they are and we know that these individuals have records.

Now, I'm not representing to you those customers are people who you want to send your kids to school with, okay? But I am representing that they are not a threat to the pari-mutuel system. At least nothing in their history would indicate that.

That talks about the history of customers, that talks about how we approach compliance and transparency, but what it doesn't talk about is monitoring a system that you basically cleaned up and have connected to the pools, and that's where Ed's efforts, Izzy's efforts, other efforts are coming into play.

We believe that we need to run electronic monitoring over the top of these systems in order to make sure that you know the activities of these individuals remain clean, for lack of a better term, and that they are not engaged in any activities that will put us collectively or individually at risk. And that's the reason that we fully and totally support what RCI is doing in its efforts.

That's why we wanted to be the first people to jump on board, because we think it's so critical to the industry. We applaud RCI. We think that's a great place to start it. We think others need to join it and we simply want to be one of the individuals regulated by it.

We think then that it, again, in the interest of candor, it takes out also all the politics of it. We think that's very important as well. It's regulators' responsibilities and jobs to help make sure that the system stays clean. We want to support their efforts in that. Not to the exclusion of others, by the way, but we certainly want to support those.

We will be doing other things, just so you know. There is one other system that we're looking at that I'll talk about before turning the microphone over to my colleagues here is that we also will be installing something called a NORA system. Some of you may know what NORA stands for. It's Non-Obvious Recognition Awareness. Basically connects people in ways much like Ed was talking about earlier. You wouldn't normally think would have relationships.

So that the fact that we do have a problem in any given pool or we do have a problem with any kind of activity, we can tie all the individuals together quickly that might have been engaged in that activity; and the reason I tell you this publicly is because it's a warning to everybody who in fact wants to engage in kind of questionable activity, don't come to Youbet to do it because that's not a place you are going to be able to do it.

We're going to put the tightest, hardest screens on our customers and our activities for one reason, and one reason only, we think it's critically important to the industry as a whole and to our business moving forward.

So that's a little bit about what we're thinking, why we're thinking, why we think it's important, some of the steps we've taken and the investments we made into it.

MR. MARTIN: I'm going to jump over Alan Ahac because he's got a series of slides, and I don't know how long your presentation is, Alan, but if it's anywhere as long as it was at the RCI board meeting last night.

Poor Craig Fravel is the general manager at Del Mar and a member of the NTRA Board of Directors. I want to make sure that Craig has the opportunity to speak and say whatever he would like to say. Craig, before Alan does a filibuster.

MR. CRAIG FRAVEL: Thank you, Ed. I was actually hoping that he would leave me about two minutes at the back end of this thing.

When they asked me to do this thing I said, well, that's probably pretty safe. At eight o'clock on the last morning of this thing with the Racino discussion going on next door, there won't be anybody here to listen. I was extremely disappointed when you all walked in here.

(Laughter)

About 10 or 12 years ago I think I was on a panel or asked to be on a panel by the folks who were running the Symposium at the time and it was on the future of the Internet as it pertained to horse racing, and so Del Mar was one of the early tracks to really jump on the Web site bandwagon and try to develop marketing strategies around that, and so I agreed that I would be on the panel.

And I mentioned to my office to someone and they said, "Well, what do you know about that?" The fact of the matter, I didn't know very much but I certainly was willing to appear on the panel because I was asked and the same person found out I was on the wagering and security panel this morning and they said, "Well, you don't know anything about that, either." And I said, "Well, that's true but, again, I'm not too shy about it."

I think the reason I'm here is mainly from both from a racetrack perspective and a little bit to Ed's point from the NTRA's perspective. Let me just start with the racetrack side of the equation.

I started in this business about 16 years ago in 1990 and candidly I had the advantage like Chuck, I think, of really knowing nothing about the business. That was what everybody always asked me, what do you know about horse racing, and the fact was I really didn't know anything about it but that helped a little bit in terms of bringing a little outside perspective to it, and as I did learn about it, trying

to look at things maybe a little bit differently, people who had been in it for 30 years, but at that time most of our wagers were on site.

I remember negotiating a deal with Nevada for simulcasting there but I think at Del Mar that was our only simulcasting agreement and separate pool agreements with Caliente and a few other locations, but we really weren't in the simulcasting business.

We quickly learned that we had to get into that business and we developed a department to handle all that stuff, but that was a dramatic departure from where we are today where we have basically virtual racetracks. We have a few more customers on site but still that will be 70 percent of our revenues that come from remote locations, both within California and around the country.

And as Chuck said many times, we don't even know necessarily where those dollars come from. And my prediction is in the not too distant future — some of you have seen some of the positioning tracking systems that have been displayed here — there's going to be opportunities for proposition wagers within the course of a race, not just who wins and loses and comes in third, fourth and fifth, but see who gets to the 16th pole the quickest from the quarter pole, and all kinds of different manifestations of wagering activity that many people around the world have probably thought of but very few have implemented to this point.

All of those are going to have serious implications for customer confidence and our ability to monitor those. So I'll tell you the situation that came up this morning at Del Mar which kind of highlights for me a bit of the issue. We had a two-horse same--owner entry run in a race which I think had five horses, and unfortunately, I guess, the entry was owned by the chairman of the California Horse Racing Board, and those two horses came in fourth and fifth in the race.

And immediately the e-mails and chat rooms, I think the Del Mar chat room on its Web site is one of the most active hotbeds of rumors in the country because of the immediate discussion that was going on about all kinds of strange betting behavior in the race, and what happened in this race, and there were rumors that offshore bookmakers had placed huge bets on this race and there was all kind of nefarious activity going on.

The first question you ask yourself when you are in that situation and you're starting to see all this stuff is, okay, well, I would like to think there's nothing wrong but we certainly can't just ignore it. Where do I go and what do I do at this point. You go to your usual sources, you go to your mutuel manager and you go to the investigators of the California Horse Racing Board there on site and you let them know that you have had these inquiries.

But the fact of the matter is even if we do an internal inquiry, review the facts of the situation and come to the conclusion that everything was on the up and up, which 99 percent of the time that is the result you get to, and we report it back to our customers, 100 percent of the time your customers don't believe you because

they think you're just trying to protect your turf, and I can tell you that's true on issues that have over the years related to late odds changes that are shown on the displays.

We go over and over and over again with the technical explanations as to why there's a delay in the posting of the odds and the running order, but customers never believe you. They just think you're part of the conspiracy.

I tell them, if I was part of the conspiracy, I really wouldn't have to have this job because I would have figured out a way to get rich a long time ago and moved on to bigger and better things. But at the time we had this incident this summer we put a call into Curtis Linnell who is on the TRPB and a wagering analyst for the Thoroughbred Racing Protective Bureau, and Curtis, who is a tremendous resource, did a terrific job of really reviewing the data on the race.

We gave him immediate access to the CHRIMS database on wagering and he went through all the betting patterns on the race, the mutuels, checked all the various and sundry things and reported back that actually the allegations of unusual wagering patterns were completely off base and basically gave the race a clean review.

My point on that is, and to a degree responding customers with reply from the TRPB that they had investigated and things looked pretty good, and the Racing Board had looked at it as well, was useful, but it highlighted to me the need in the long haul for an authoritative voice on all sorts of wagering and other integrity issues relating to the game.

I think to allow customers to have sufficient levels of confidence in us, we have to demonstrate that not only are we capable of reviewing things but that there is a sufficiently independent and authoritative organization out there that can be the ultimate arbiter of those kind of decisions, and to a degree track management does have a vested interest in making sure that, or at least portraying the game as on the up and up, but we are a little suspect simply because we are maybe overly confident at times, and I think the Breeders' Cup Pick-6 scandal was a classic case of that.

I had said for years that upon representations by various tote companies there's no way anybody could get in and manipulate the mutuel pools. Well, in 2002 we found out that that was absolutely untrue and I had been told for years that there was no way that anybody could do past posting and found out about six months after that that somebody was past posting in New York.

I think we're all obviously very supportive of proceeding on these cooperative paths. I'm not the least bit, as an NTRA board member, not the least bit discouraged or in fact pleased to hear that the RCI has taken the action that they've taken. I sit on the NTRA board that yesterday approved a half million dollars worth of enhancements in its budget to proceed down a similar path but with the idea of working cooperatively with the other organizations in the business,

and the NTRA board at its last meeting approved about a million dollars towards the development of these projects.

All of whom I think took these actions not by way of saying to the rest of the industry we're just going to go on our own but I think in each case it has been slower than any of us would have thought. I'm think we had some fits and starts. I think the original plan was to move these wagering transaction protocols early on, and we've subsequently found that that path is going to take a lot longer than anyone thought, so the need to move forward on as many different fronts as we can and to coordinate these efforts has improved dramatically.

From my perspective, this industry has the ability, when it decides to do it, to move effectively and cooperatively in a number of ways. I think the Medication Testing Consortium that Scot chairs is a classic example of that. People thought there was no way two years ago that we would be achieving uniformity in medication rules and, amazingly enough for those of us who sit on that panel, we're very, very close as to that goal at this point, much closer than actually the general public really has a feel for.

I think that's just one example of how we can accomplish these things when we put our minds to it and I think with the RCI's efforts, the NTRA's efforts and the cooperation of all these various entities, we're going to get there.

I'll move on to Alan and his voluminous presentation.

MR. MARTIN: Alan Ahac, with ESI Systems Integrity, they do independent monitoring of approximately, I think it's \$20 billion, various types of gaming handle worldwide. The company is deeply involved in gaming, in lottery, provides an overlay system in Canada and I don't want to steal your thunder and happy to have you as a partner of RCI, Alan, so I'll turn it over to you with your 96 minute PowerPoint presentation.

MR. ALAN AHAC: Thank you for setting everyone's expectations on my presentation. I will try to keep this brief.

I guess what I would like to do is to step back a bit and provide you with, first, a bit of perspective. As Ed mentioned, our company's involved with many forms of gaming, and when I read about our topic today of policing the wagering system I thought it might be interesting for everyone to understand what other gaming industries do very briefly, and I guess second to that I would like to provide you a little bit more detail about what we're specifically planning to do with the RCI Integrity Services.

I think Ed briefly mentioned this, but I'll give you a bit of background on our company. Our whole purpose in life is to provide software for the regulation of gaming. That's certainly a niche type of market, but it certainly provides a great deal of focus. We work in government lotteries, pari-mutuel world.

The technology that we talked about has been studied greatly for potential regulation of Internet wagering, monitoring of sports betting, casino monitoring and wagering information systems. Again, just to give you some perspective on what we do, our technology monitors about \$20 billion a year in wagering, almost all of that in real time. Our customers are worldwide.

And specifically in the pari-mutuel world our real first foray into this particular sector of gaming is in Canada where we've deployed a system that monitors essentially all pari-mutuel wagering and now across the country. As well, our systems have been deployed in the State of Florida and we have been monitoring hubs for a number of years now, and for the last year or so we've also been doing monitoring NYRA's wagering through our agreement with United Tote.

I think the topic today, how do you police the wagering system, when we talk about that, the fundamental question is really is the wagering system behaving the way it's supposed to, and the questions that you are trying to answer, does it follow the rules?

When you publish your rules of how a trifecta pool works, is the wagering system following that? And not only is it following the rules, does it have effective mechanisms in place to make sure that people who attempt to break the rules in some form or another are being refuted?

So how do you insure that a wagering system is behaving the way it's supposed to? Fundamentally, in different forms of gaming, fundamentally, there's two approaches and most gaming uses some combination of the two. The first approach is what I refer to as test and freeze. Get somebody to thoroughly test the wagering system so that we have high level of confidence that it will operate correctly, that it will behave correctly, and then we freeze that version and don't allow any changes to it, put it into production, and if it needs to be changed, it has to re-undertake a testing process.

The other type that we're particularly familiar with is continuous monitoring. In that particular case what you're doing isn't necessarily — what you're trying to do is, as the system is being operated in production, you're continuously monitoring it to make sure that it's behaving the way it's supposed to behave.

So it really is a process that of monitoring that's being undertaken while the wagering systems are in operation, and in most forms of gaming both of these or some form of combination of these types of approaches are taken.

Again, I talked briefly, the test and freeze approach. Very common with slot machines, for example, in the gaming industry. You certainly may have heard of testing laboratories like GLI or TST. They are independent test agencies that undertake the testing process against specification that stipulates what good behavior and correct behavior is.

And then once it has been approved, a lot of effort is put into making sure that the version of wagering system that was tested is frozen and can't be changed.

The difficulties in this approach and, first, it's very difficult to specify all the correct behaviors ahead of time and, second, it's very hard to design a complete set of tasks that guarantees the wagering will behave correctly in all cases.

Really the intent of the continuous monitor system is then to, on an ongoing basis, once that software is in production, that wagering system is in production, is to make sure it's behaving correctly once again according to the rules.

Most monitoring systems are real time; that is, every wager, every transaction that occurs is checked as it's received and if incorrect behavior is detected, alerts are raised. And certainly the monitoring system has to be independent of the wagering system.

In monitoring systems in lotteries these monitoring systems are typically called ICS systems, Independent Control Systems. In the casino world they are called Central Monitoring Systems, typically. Sports betting often call them Risk Management Systems, and these monitoring systems are typically required by and most often operated by the actual gaming regulator.

So what do these things specifically do? They independently process all these transactions from the wagering system and check the rules. In particular in the pari-mutuel context it independently determines winners and payout amounts and audits the takeouts. And very importantly, it also maintains an independent database of all the wagering and information so that if investigation is required, this could be undertaken promptly and in fact independent of the wagering system.

In the pari-mutuel world, as I mentioned, these have been deployed in Canada. Scientific Games contracted us to monitor all of their sites after the 2002 Breeders' Cup incident.

More recently Florida, the State of Florida division of pari-mutuel wagering adopted this, our technology, including monitoring all three of their hubs, and for the first time actually as well that system provided a central database that consolidated all the information amongst those, information from those sites and consolidated it into a central location. That work is in full operation now.

We're also, as I mentioned, in NYRA, when it went out to, for its RFP for its last wagering systems procurement they undertook, they required such a system, and we're happy that we're able to work with United Tote in providing a capability to NYRA.

Let me just give you a picture of what we've done in Florida because it forms the basis of really what's going to be happening with this new national facility that Ed has introduced. What there is, there's three tote hubs. You can see them as orange dots on that schematic. They are all connected over a high speed secure link to a

data center in Miami that has three monitoring systems plus a central database, and that, those systems in fact are accessed, predominantly operated by the state regulator's office in Tallahassee.

What you can see here is largely due to the evolution of high-speed secure communications. In this structure we're able to have a fairly distributed type of architecture while still meeting the need.

Let me now talk specifically about what we're planning to do as partners with the RCI relating to a national monitoring center. In essence, there will be two data centers that will contain the monitoring systems. Those specific locations haven't been determined yet, but we expect there to be one in the east and one in the west.

Each of those data centers will be connected to each of the major tote hubs that are being monitored by our systems. And there will be separate from those two data centers a national office where the systems in fact will be operated.

There will be a group of people we term "compliance officers" working in those offices. Those compliance officers would be in essence found and hired and managed by the representative of the regulators and really are acting as agents of the regulators.

At the outset there will be likely two or three of those people; at full deployment, we expect a requirement for about nine on staff.

In essence, when an incident comes up, alert is raised by the monitoring system, those compliance officers would coordinate a response, typically involving the tracks, local regulators and more than likely the tote operator where the information will be shared, a response will be to coordinate, determine if a potential error or potential fraud has occurred.

The intent is that ultimately this office, as I mentioned, will have nine compliance officers plus administrative and some technical support people. Perhaps a staff of 13 people.

I think Ed mentioned this. The partners in this are obviously ourselves, RCI and MTI, Monitor Technology, those of you who know Izzy Sobkowski.

One of the things that's important to us as we've sort of started to understand this industry better, certainly one of the next levels of monitoring that we believe is required here, in fact, in the gaming industry worldwide, is what we call transactional pattern analysis.

Really many types of fraud and I think there's many interesting examples even Chuck was tossing around. Specific example might be money laundering.

Oftentimes there's no hard rules or easy ways to specifically pinpoint the case of money laundering; however, usually what is required is some analysis of the patterns of wagering to determine if something unusual is occurring.

And those patterns will adapt. The perpetrators will often adapt in the way they are placing money, and they'll adapt in the way they'll in essence, take the money out.

We felt it was important to layer this type of technology onto what we've currently been doing to be able to detect those types of fraud.

I'm going to very quickly show you how this specifically will work. It's a case of one tote hub, various ticket issuing machines and monitoring systems that might be residing at the data center. Just to quickly give you an idea how this works, firstly, these monitoring system are connected by a secure, encrypted network link to make sure no one can intercept the information.

And as I mentioned before, a copy of each transaction is sent to the monitoring system, and that means every transaction. That's very important.

So, for example, if I place a bet at the TIM, that transaction typically would go to the tote system, but the key thing is that immediately after processing by the tote system, a copy goes to the monitoring system. Similarly, if you were to import monies from a guest tote, this, again, would be a transaction that goes to the tote and a copy of it would go to the monitoring system.

When betting's closed that's in fact typically initiated, transaction initiated out of the tote system, the monitoring system, since it's been keeping in essence a copy of every wager and totaling money that are in the pools, can independently calculate the payout price as compared to the results and confirm that the price is valid.

When race results are in, similarly, a copy of the results transaction has passed a monitoring system, results are compared and prices can be confirmed. And, importantly, independently the winning tickets can be selected and subsequent to that the caches of the winning tickets can be monitored.

Simple example of a simple case of fraud. Let's say that a past-posted wager is placed and due to some error the tote system doesn't catch it so the bet would have come in and a copy of it would have gone to the monitoring system. Monitoring system has rules that relate to those types of violations.

An alert would be received. A compliance officer would then likely phone the track and the tote operator, perhaps a state regulator, to coordinate a response how that could have happened and what are the implications.

Obviously, if it's a winning ticket, one would probably very quickly want to make sure that it couldn't be cashed and there would be an investigative effort obviously to try and find out if this was a random act or an act of collusion, that type of thing.

On top of that there's a variety of reports and tools that can be provided by the technology. I won't spend too much time. Just a prototypical screen.

This is kind of interesting. One of the things our system provides is a graphical illustration of the payout prices, so what you see here are the prices on each of the — in this case I believe it's a Race 3 to-win pool. The payoff price over the course of time.

You will see on the right-hand side of the screen when the symbolization turns a little black dot that indicates betting has been closed and clearly you're kind of very concerned about things, major jumps or changes in this graph, particularly after betting is closed or even immediately before betting is closed.

Obviously, the purpose of this type of tool is to allow people to see if there's significant odds manipulation or that type of thing.

Again, I mentioned briefly, and I won't spend too much time on the particular details of the technology, but we think it's important to layer on top of what we have been doing the type of technology that can deal with some of the harder and more complex firm types of fraud such as money laundering and various types of wagering fraud that depend on transactional pattern analysis.

In essence, this uses jurisdiction pattern detection to raise alerts to the compliance officer and allow you to then gain, respond if unusual activity is determined. That's really the technology behind it.

Let me talk a little bit more about the company, RCI Integrity Services. What we're proposing to do with the RCI is to form an independent U.S. corporation to provide services for monitoring wagering activity and ultimately to insure the integrity of wagering activity.

It's interesting already that we probably have to adapt our mission because particularly with the adoption of net pool pricing and international monies now coming — more international monies coming into U.S. pools, Canada is a great example, that really this service is quickly becoming an international service. As the industry legitimately seeks to offer its wagering product internationally, obviously our integrity capabilities, security capabilities are going to have to adapt to that.

I won't spend too much time on this related, describe the objectives of the business.

MR. MARTIN: I want to leave some time for questions.

MR. AHAC: This is probably my last one. I think, again, to summarize what I think has already been mentioned, we're happy that we have two launch customers, Youbet and Scientific Games.

As Ed mentioned, within six months this business will be monitoring more than half of the pari-mutuel wagering in the U.S. Ed mentioned model rules and I think the industry itself has spoken and suggested that this type of thing needs to be in place, and we certainly hope to see other customers joining this service very soon.

Ed, that's my 20-minute presentation.

MR. MARTIN: Pretty good. Ninety minutes into 15.

I want to leave some time for questions. So we'll turn it on open to the floor; otherwise, the four of us will have to start talking again.

A VOICE: Question probably for Alan. Is there an impact on double hopss for monitoring? Is that possible?

MR. AHAC: In essence, the monitoring system monitors each tote hub and it consolidates data between hubs. So in the double hop case, in fact, really three different tote hubs, two to three different types of tote hubs involved minimally; and as long as there's a monitoring system on each one, you are able to monitor what's coming in from one hub, what's being collected at one hub as a wager and what's coming in as an import for the next hub and what's coming in as an import to the next hub and what's coming in as an import to another hub.

And then through the central facility you can consolidate those, the information between those three to make sure they balance in essence.

The answer to your question is the monitoring system can see what is on each tote system. Certainly if a tote hub is not connected to the monitoring system, we would only see the import, we wouldn't see the individual wagers.

MR. MARTIN: Everybody still awake? Any more questions?

A VOICE: My question would be for Alan again. Have you noticed any changes in — I know we're all concerned about wagering activities that change the odds at the last minute, Craig had mentioned. Have you noticed at any of your jurisdictions that pattern has changed or improved significantly through your — or are we just still in the reactionary stage to investigate things after they look funny?

MR. AHAC: Again, without offering a great deal of analysis, I can say that the hubs that we have been monitoring for longer periods of time, surely there's been improvements in odds fluctuations and I think the way these did, the adjustments that the tote vendors have made in how they are providing in the pools, in the pool information in essence has reduced the fluctuations, particularly after the close of betting.

There's no doubt there's an improvement, but frankly, communications fluctuations still create delays and it still occurs.

MR. FRAVEL: I might add to that, Doug, I think part of what's been going on there's clearly been technical advances and a little better cooperation amongst tote companies and means of trying to get money into the pool more quickly and, candidly, we in the last three years of racing, the two years prior to this year we were answering questions about layout changes virtually every day. This past summer I don't think we had a single occurrence.

I think that's partly a function of the technical issues, but there's also some self-policing going on amongst the rebate shops that tend to be the sources of most of the late odd changes, and when I say that, I think they are basically pushing their wagering back a little bit. They don't seem to have that kind of negative inference. I think they probably realized that was probably counter their own interest ultimately if public confidence was impacted.

I'll also tell you that we monitor, every time we got an inquiry on those, our pari-mutuel auditor through our pari-mutuel department. On the racing board we monitored all those checks precisely when money came in, and it was always within standard parameters of what you would expect. It has changed dramatically in the last year.

MR. MARTIN: I think it's important to know that, first of all, the technology is driving a changing world around us all in so many aspects of our lives and what we did, sent a letter prior to the NTRA board meeting to Commissioner Van Cleef and informed him to what our intentions were at RCI and invited the NTRA to participate and appoint some representatives from the industry to participate and help advise us on the advisory panel at the company.

We, also, several months ago, reached out to some of the directors of the TRA to see if there was any desire to explore feasibility of how the great talent that's in the TRPB and the great talent that's in the various state regulatory agencies collectively through RCI can possibly better work together and see if a possible reconstitution and strengthening, it's not a criticism what I'm saying, a reconstitution of strengthening of TRPB could possibly help us pool some of our investment.

But the key here is independence. And the question of independence, and probably Chuck knows this as an old newspaper person, how many times have we watched 60 Minutes or any one of those investigatory TV shows where they ask you why did you hire somebody who was being paid for by the person; is that truly independent? The key is independence, and if you're going to have an independent monitor, that independent monitor, the position that the regulators are taking, cannot be housed in a trade association of the industry. It should be independent.

And certainly as regulators we're independent, various configurations of that and that's why we took the step that we took to go in the direction that we did. I think it's very encouraging that NTRA is willing to invest. I think that the TRA move yesterday is encouraging.

What I think is the danger here is our business model is based upon providing a service, charging fairly for it and helping to work, working with the industry to develop it so it adapts to meet the needs of the industry rather than building multiple systems, and that could be a very costly duplication for everybody.

A VOICE: Besides the necessary changing to the model rules in the work, do you anticipate anything to do legislatively to change the existing system?

MR. MARTIN: The system is being offered as a product to the industry. States who are members of RCI will be able to participate in it. If a state wishes to contract with the company as opposed to require its tracks, there's three ways customers will come to this entity, voluntarily because they feel it's the right thing to do, or if the state or jurisdiction were to require an independent monitor, then this company will compete and provide that service with, if anybody else is out there to do it.

And the third way would be if the state decided, well, we don't want to require the industry to do it, we're going to do it ourselves and go to the legislature and the legislature gives them the resources to do it.

As we proceed with this you will see that the financial hit is not a heavy one.

Well, with that being said, thank you all for coming this morning and it's time for coffee and have yourself a drink. Thank you.

(Applause)