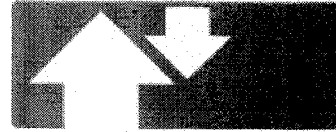


betfair



REVOLUTIONISING BETTING

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**Review of issues related to Commonwealth
Interactive Gambling Regulation**

**Submission by Betfair
to the Department of Communications,
Information Technology and the Arts**

2 May 2003

Summary

Betfair welcomes the opportunity to make this submission the objectives of which are to:

1. propose that the existing 'excluded wagering service' exception contained in S.8A of the *Interactive Gambling Act 2001* (the "Act"), save for one amendment as indicated in paragraph 2 below, should remain;
2. propose that the restriction on betting 'in the run' should be removed (i.e. betting in the run on the outcome of sporting events after the beginning of the event should be an exception to the prohibitions in the Act), as it serves little purpose in minimising the harm associated with problem gambling, and that the Act should be amended accordingly. In fact Betfair submits that betting in the run can act as a valuable hedging tool for the responsible gambler. In addition, betting in the run is available through another medium (i.e. the telephone) so the interactive restriction is anomalous;
3. demonstrate why betting exchanges do not encourage problem gambling but instead can help to promote responsible gambling; and
4. refute some of the recent claims made about Betfair and address some of the misconceptions about betting exchanges in general.

1. Introduction

Who is Betfair?

The Sporting Exchange Limited (trading as Betfair), a company registered in the UK, was founded in 1999 and began trading in June 2000. Betfair is a licensed bookmaker in the UK. It has grown rapidly since its inception and in January 2002 it completed the acquisition of Flutter.com (the other leading betting exchange at that time). Since then it has consolidated its position as the global betting exchange market leader. Betfair is based in West London and now employs almost 200 people. It is widely recognised as a spectacular success. In December 2002 its co-founders won the prestigious Ernst & Young Emerging Entrepreneurs of the Year award and in April 2003 the company won a Queen's Award in the UK for Enterprise in the innovation category. We believe that this is the first time that this award has been made to a company in the betting or gaming sector.

How does a betting exchange work?

A betting exchange is a market place where individuals with opposing views on an event express those views by making fixed price bets between themselves. It operates in a manner resembling a stock market. On a stock market a trader can buy or sell a commodity, and similarly on a betting exchange a player can either back or lay an outcome.

In the case of the Betfair exchange this is predominantly done on sporting events.

A player is required to open an account with the exchange before placing a bet and all bets are cash collateralised so that a player is required to deposit with the exchange his or her maximum potential loss on the relevant event when striking a bet.

The betting exchange acts as stakeholder which removes any danger of a player failing to honour a liability. The exchange in its role as stakeholder holds the client funds at risk on a bet, until the outcome of the relevant event is determined. Once the result has been determined the winnings are paid to the winning player. Typically all bets are pooled so a user may be betting against one or several other players and the counterpart(y/ies) to the bet are anonymous to the player (but importantly not to the exchange). The betting exchange's profit is derived from a commission levied on the player's net winnings per market. Betfair's commission is levied at between 5% down to a minimum of 2% for the biggest players.

Betfair complies with all laws applicable to UK bookmakers

Why are betting exchanges popular with players?

Betting exchanges offer players much greater choice and value than that offered by conventional bookmakers. On Betfair for example a player:

- can bet for or against an outcome. With a conventional bookmaker a player can generally only bet for an outcome;

- can ask for better odds than those currently on offer about an outcome or offer or request his own odds. Although a player can request better odds from a conventional bookmaker, it is not common practice;
- does not have to accept the comparatively large margins built into the prices offered by a conventional bookmaker or a TAB;
- can hedge a bet to minimise a potential loss or lock in a certain profit before the outcome of the event has been determined – both examples of responsible gambling in the sense that losses can be restricted and profits can be guaranteed before the outcome of the relevant event has been determined;
- is less likely to be subjected to a bookmaker’s arbitrary rules: he knows he will always be paid out and not have his account closed for being too successful. The bookmaker in this case (i.e. the betting exchange) takes no market risk and is not interested in the outcome of the event; and
- can easily access details of what has been traded on every outcome at what prices. All activity on the exchange is completely transparent. Access to similar information with a conventional bookmaker is generally closely guarded by the bookmaker.

Betfair’s recent profile in Australia

Betfair has recently generated much Australian press coverage and the Appendix to this submission contains some examples (together with an article from the UK Racing Post). However, not all parties have welcomed our arrival in Australia.

We have had verbal confirmation from the Australian Broadcasting Authority (the “ABA”) that a complaint regarding Betfair was recently made to the ABA in relation to Betfair’s service which was subsequently investigated by the ABA and a referral was made to the Australian Federal Police. We have received no official notice to date about the complaint, investigation or referral by any Australian government agency or law enforcement body other than this telephone confirmation with the ABA initiated by us. We had no previous knowledge of the matter until it was referred to in the Australian press.

Although commercially motivated third parties have sought to make capital from the matter, Betfair believes that its procedures address the issue in question. Betfair strongly believes that these third parties have responded in this manner due to a perceived threat posed to their businesses by the success of Betfair’s operations.

2. Betfair’s existing regulatory framework

Betfair is a licensed bookmaker in the UK, its principals having passed the necessary probity requirements which require them to be ‘fit and proper’ persons.

Betfair is working closely with the UK regulator, the Department for Culture Media and Sport (“DCMS”), in relation to a forthcoming betting and gaming bill which is expected to come before Parliament in the UK in 2004. This general overhaul of current betting and gaming legislation will include the regulation of betting exchanges. The DCMS recognise that the current legislation (primarily the Betting, Gaming and Lotteries Act 1963) which covers bookmakers (which term includes

betting exchanges) is outdated and in need of modernisation. Betting exchanges will be specifically catered for in this new legislation. It is envisaged that the legislation will come before the UK Parliament in 2004.

In the meantime Betfair has voluntarily adopted a number of self-regulating measures which may or may not form part of forthcoming legislation. These currently include:

a) Promoting responsible gambling - Betfair is working closely with Gamcare who are a UK registered charity seeking to promote responsible attitudes towards gambling. As a consequence Betfair will shortly introduce mechanisms on its website that will allow Betfair users to:

- set self-imposed maximum exposure and deposit limits – once set these limits will be fixed for a set minimum period; and
- choose to self exclude permanently, or for a specified period from Betfair.

Self-regulating safeguards such as these are rare among conventional bookmaking websites in the UK. Betfair also provides a link to Gamblers Anonymous (“GA”) on its website – GA does not affiliate itself with gambling operators.

Betfair takes the issue of underage gambling very seriously. Users must be over 18 to register with Betfair.

Betfair goes further than it is currently required to under UK law to ensure that problem and underage gambling are addressed and will be committed to complying with all regulatory requirements in this respect in any jurisdiction where it is licensed.

b) Ring-fencing of customer funds – all customer funds are held by a stand-alone subsidiary of The Sporting Exchange Limited. This subsidiary exists solely to hold client funds and undertakes no other functions. This means that customer funds cannot be mixed with operating funds and, in the unlikely event that the operating company were to become insolvent, a liquidator would have no claim on customer funds held by the subsidiary company. There is currently an implied trust in favour of our clients in place in respect of the funds held in the subsidiary company and we will shortly be formalising this into an express trust arrangement with our bank. In the UK there has been several high profile examples of conventional bookmakers with no ring-fencing arrangement in place failing, with players suffering losses as a consequence.

In any event, because Betfair takes no market risk it is less likely to fail than a conventional bookmaker.

c) Safeguarding the integrity of sport – Betting exchange critics claim that the exchanges represent a new threat to the integrity of horseracing in particular, because they have introduced the facility to bet against a horse. However spread betting has for many years allowed exactly the same effect to be achieved by ‘selling’ a horse on a given index; similarly betting on the rest of field with conventional bookmakers achieves the same result – i.e. it singles out one horse who the player is looking to oppose.

Betting exchanges should not therefore be condemned as a massive new threat to integrity. On the contrary, Betfair believes that properly regulated betting exchanges can provide a massive help to the authorities in policing the integrity of horseracing and sport in general.

Betfair has since its launch been sharing information on unusual betting patterns with the UK Jockey Club (the “JC”) in a manner totally unprecedented amongst conventional bookmakers who are notoriously unwilling to cooperate with sports’ governing bodies in order to protect the information networks on which they depend. Betfair is also now in the advanced stages of talks with the JC to agree a memorandum of understanding that will facilitate the passing of even more information (including names and contact details of suspected offenders) to the JC if the parties believe that the JC’s rules of racing may have been breached. The resulting change in Betfair’s privacy policy is something to which Betfair users will shortly be required to agree if they wish to continue using its services.

Such levels of cooperation are made possible by Betfair’s extensive audit trail where every transaction made on the exchange is recorded indefinitely and can be identified with an account holder (as opposed to those of conventional bookmakers which obviously accept cash). The initiative has been lauded by the JC and it demonstrates a level of cooperation never previously shown by conventional bookmakers in the UK.

The JC initiative is something that Betfair would repeat without hesitation with appropriate regulatory bodies elsewhere.

Addressing common misconceptions about betting exchanges

“Betting exchanges provide a vehicle for money laundering”

In contrast with conventional betting operators, no cash betting is possible on betting exchanges. Deposits on Betfair are only possible by credit or debit card, by way of bank transfer or by cheque. All money bet via Betfair has already been cleared through the banking system. In addition Betfair’s audit trail records every transaction indefinitely and each can be traced back to a relevant Betfair account holder.

Betfair has in place internal checks to monitor payment and betting transactions. Any payment request that exceeds the amount deposited to the relevant account to date is manually checked and Betfair will report any suspicious payment requests to the relevant authorities in the UK. Betfair’s records are open to the UK authorities if they believe that any criminal activity has taken place through the Betfair exchange.

“Betting exchanges will lead to the demise of bookmakers and racecourse attendance will suffer as a consequence”

The growth of betting exchanges in the UK has not adversely impacted on UK racecourse attendance. Betfair believes that the use by on-course bookmakers of betting exchanges strengthens the on-course market – a view recently endorsed by the National Joint Pitch Council (the body that is responsible for the organisation of betting on racecourses in the UK).

The ability by on-course bookmakers to access off-course money through the use of betting exchanges, which has been ratified by the Horserace Betting Levy Board (the body responsible for the funding of racing in the UK), gives the on-course market access to new money and the hedging mechanism it provides allows on-course bookmakers to stand more sizeable bets. A practical example that has been given in the racing press by a leading UK on-course bookmaker is where a horse is trading at, for example, 6.0 on-course. If he is able to back this horse at 7.0 through the exchange, he can now come back and offer 6.5 to players on-course. This suggests that prices available at the racecourse are actually better than they would be without the use of exchanges. A stronger on-course market with better prices available encourages people to come racing rather than the opposite.

Separately, an increasingly large number of conventional off-course bookmakers (including some in Australia) now legitimately use betting exchanges as a hedging mechanism and a means of reaching an expanded market – thus strengthening their business.

In addition conventional bookmakers and TAB's offer to their customers a variety of products (including multiple and exotic bets) that are not available to betting exchanges users. The arrival of betting exchanges is not likely to cause demand for these products to disappear.

“Betting exchanges contribute far less to racing (and the government) than conventional bookmakers/TAB's do”

- a) Although this is arguably the most common claim by those with a commercial interest to protect, this is completely untrue, and in fact it is arguable that the opposite is true: every dollar in the player's pocket generates more for racing if recycled through the exchange than it does if recycled through a TAB. With its higher margins, the TAB simply provides a more effective means of relieving the player of his or her dollar more quickly, for distribution elsewhere.
- b) The argument put forward by TABs is simplistic. It does not compare like with like and ignores the multiplier effect that betting exchanges can have on turnover. Betting exchange turnover first represents a figure that is doubled (by virtue of recording the stake of both the backer and the layer), and secondly generates far greater churn because of the existence of a far lower margin (see the third article from the UK Racing Post in the Appendix in relation to the lower margins available on Betfair compared with conventional bookmakers in the UK). Despite the success of Betfair in the UK (in excess of £50m of matched bets per week) conventional bookmakers are still recording record turnover.
- c) In addition there has been no tangible evidence shown that horseracing funding in the UK has suffered as a result of the success of the betting exchanges. Betfair is one of the largest sponsors of horseracing in the UK and Ireland and is the main sponsor of Fulham FC, a premiership soccer club. Voluntary contributions such as these also form a vital part of the funding of sport.

3. The Interactive Gambling Act 2001 (the “Act”)

Existing 'excluded wagering service' exception should be maintained (but with one amendment)

Betfair submits that the existing 'excluded wagering service' exception contained in section 8A of the Act, with one amendment (see below), should be maintained in the Act.

Additionally, Betfair submits that the availability of this exception should be maintained in the Act and not restricted in any manner.

'In the run' betting should be permitted on wagering services

Betfair strongly believes and submits that the prohibition on betting 'in the run' on sports betting events contained in section 8A(2)(a) of the Act is inappropriate and the exception to the 'excluded wagering service' exception contained in section 8A(2)(a) should be removed. Betfair submits that the existing exception for an 'excluded wagering service' should be extended to permit in the run betting.

This sub-section prohibits a bet on the outcome of a sporting event after the beginning of that event. Betfair offers in the run facilities to players located outside Australia which are provided as an add-on to specified events in a seamless manner. In other words, once a football game or a horserace begins, the event is turned 'in-play'. This facility is extremely popular and although it has been offered by conventional bookmakers in the UK for many years, the dynamic nature of a betting exchange is particularly suited to this form of betting.

Betfair understands that the restriction was included in the Act as a measure to prevent players betting without due care and thought, and to discourage irresponsible gambling. However, Betfair's 'in-play' facility in many respects has the reverse effect and encourages responsible gambling. For example, it allows a player to minimise a loss by hedging a position during an event thus reducing his exposure on the event. Without access to in-play betting a player is stuck with a bet once the event starts. The exposure on an ill-considered bet cannot be reduced or eliminated, nor can a profit be locked-in if the event is going the way of the player's selection.

The existing prohibition on in the run betting results in practical and operational anomalies based on the technology used. For instance, it appears anomalous that a player can bet in the run by telephone (pursuant to section 5(3) of the Act) but not on-line. This means that betting in the run is readily available to the player but at an increased cost to the operator providing the service.

Further, it is inconsistent with the philosophy of prohibiting in the run betting on sporting events over the internet when in the run betting is currently legally available through licensed operators and telephone operators.

4. Conclusion

Even critics of betting exchanges in the UK recognise that exchange betting is a significant innovation. It is a more efficient form of betting than that offered by conventional operators and cannot be ignored. Further, betting exchanges offer better options than those provided by betting operators by telephone and offer better odds to players than traditional forms of gambling.

Claims that betting exchanges pose a threat to the integrity and funding of sport are commercially motivated and are not supported with evidence. The proper regulation of exchanges represents an opportunity to the future funding of sport in Australia and for taxation revenue, as well as protection of players and various other opportunities. Unregulated off-shore betting exchanges do represent a threat because control will be lost resulting in:

- a) an inability to put in place measures to prevent irresponsible gambling,
- b) a possible threat to the integrity of sport; and
- c) revenue generated on sporting events not finding its way to those providing the product.

Because betting in the run is such a strong feature of exchange betting, an on-shore tax paying betting exchange will be at a serious disadvantage to an off-shore competitor who is able to offer this service. For this reason Betfair believes that removing the prohibition in section 8A(2)(a) of the Act is essential to the future success of properly regulated on-shore betting exchanges.

If you have any questions about this submission, please contact Mr David O'Reilly, Legal Counsel for Betfair on + 44 20 8834 8212 or email david.oreilly@betfair.com.

The Sporting Exchange Limited (trading as Betfair)
2 May 2003

Appendix

Punter the big winner

By TIM HABEL.

28 March 2003

Herald-Sun

The ANALYST BETTING exchanges will be the dominant form of horse racing wagering in five years.

That's the prediction of renowned betting analyst Mark Read.

Read said yesterday betting exchanges were "inevitable, a fact of life".

"It is the evolution of wagering. It will be a boon for our industry," he said. Read said the punter was the big winner. "The forgotten issue is that in any other business the consumer is king. TABs are exploiting customers," he said.'

Read said the average TAB commission on all bets was 18 per cent or a return to player of 82 per cent.

"Compare that to gaming machine operators. They return up to 94 per cent to players. (TAB) Wagering can't compete in the long-term," he said.

Read claimed Tabcorp and bookmakers should embrace the betting exchange concept.

"The TAB model of 25 years ago is redundant today. There are more sophisticated players who want to use globalisation and better technology," he said. "Any bookie worth his salt should embrace it."

Read claimed every professional punter in Australia was using Betfair.

"TABs can't expect to have a monopoly. They need to get in the real world. If it's too hot in the kitchen they should get out," he said.

Read said the betting exchange model was "modern technology that takes out the middle man".

"The bookie used to be the broker. Now there is an electronic broker," he said.

Read said integrity was safeguarded because records were kept of every bet by betting exchanges.

The Sydney Morning Herald

Sport - The Form - Betfair - no wonder they're worried.

By Peter Lawrence.

17 April 2003

The Sydney Morning Herald

WEIGHING IN

The powers that be want the raw deal for players to continue, writes Peter Lawrence.

A forum was held last week at Randwick to brainstorm some ideas on how to deal with Betfair. The usual suspects and doomsayers appear on the Racenet website delivering their speeches in full.

Let me warn you first, though, no toastmasters here. The drab delivery is only matched by the dullness of the content.

The most extraordinary comment came from TAB chief executive (wagering) Peter Kadar: "What is critically needed is for the industry as a whole in Australia to immediately launch a consolidated campaign against betting exchanges."

Does Peter expect players to join in this consolidated campaign? The problem for players is that over the past 10 years an unlikely alliance has been struck between raceclubs, the media, bookmakers and the TABs. The aim of the alliance is to maintain the status quo and, in the process, screw the player as fast as they can.

Now a new medium for betting has emerged that, God forbid, may give the punter an even break.

The response from the alliance? Hold a forum to discuss how to make this evil idea illegal, not a forum on how to rise to the challenge of this new business venture. Strangely, almost everyone at the meeting would vote Liberal and claim to be a believer in "free enterprise". Unless, of course, it applies to their own enterprise. Then we need government intervention.

Bookmakers in Australia will have no one to blame for the popularity of Betfair but themselves. Their representatives' philosophy at these gatherings is about closing rings and keeping out anyone with any dash. Incredibly, the bookies' rings in Sydney and Melbourne are closed.

Now we learn Queensland bookies are trying to close the Brisbane ring.

The prices being bet in Brisbane and Melbourne are an embarrassment to a bookmaker. Mark Read can put up a market on his website at noon each day set to 127 per cent, yet Melbourne bookies can't better 150 per cent for an opening call. It is commonplace in Brisbane to jump with the call above 140 per cent.

The worst thing in all this is that no media outlet seems to care about the punter. How has the media been roped into this coalition of those willing to pillage the industry? Well, of course, the TAB has bought up almost all the media outlets. That doesn't help.

The TAB's new punting "product", called Spinner, is specifically designed for the complete moron who knows nothing about racing and wants to have a bet. Keno, pokies, Spinner, the Cannington Dogs. What's the difference between gambling and gaming again, Minister?

The media almost never mentions that the TAB takes millions off punters each year by rounding down. Not just to the nearest five cents, but to the nearest 10. If the right dividend is \$1.99, the punter gets \$1.90. How is it that no one cares less about the punter when he makes up 95 per cent of people involved in racing.

Punters keep racing going. Without the punter there would be no TAB. Now, after years of being ripped off, the punter is about to fight back through a new way to bet.

I say that if the TAB and the bookies can't compete with Betfair, betting to 110 per cent, then so be it. Let them perish. If they can't come up with something more imaginative than Spinner, they deserve to perish. P Lawrence, Byron Bay, NSW.

The Racing Post

Cheltenham - first blood to exchanges

Published: 01/03/2003 (Comment) David Ashforth

WHAT price is Best Mate for the Tote Cheltenham Gold Cup - 6-4 or 2-1? It's a big difference, and it's the difference between the traditional bookmakers' ante-post prices and the new world of the betting exchanges.

Betfair, with Betdaq and Sporting Options at the end of their coat-tails, are knocking the Big Three into a cocked hat.

The exchanges are going to do massive business at Cheltenham - if their systems can stand the strain - and by early yesterday morning Betfair had already matched more than pounds 380,000 in win bets on the Champion Hurdle and pounds 250,000 on the Gold Cup.

Betdaq don't say how much they've matched, but the fact that no price was available for backers of Intersky Falcon, second favourite for the Champion Hurdle, was an indication of how far they lag behind Betfair.

Sporting Options, with less than pounds 17,000 matched on the Champion Hurdle and less than pounds 15,000 on the Gold Cup, are still minnows.

Despite their higher commission rate - a maximum of five per cent on net winnings, compared with Sporting Options' maximum of three per cent and Betdaq's two per cent - Betfair dominate the exchange market, at least on UK horseracing.

Even if Betfair stood alone against the Big Three, the comparison of prices and betting percentages is extraordinary.

No wonder they are squealing so loudly about unfair competition and bumpy playing fields.

Ladbrokes, William Hill and Coral are united on Best Mate's price - 6-4 all round - while, yesterday morning, 2.05-1 was available on Betfair. Admittedly, it was only available to pounds 108, but another pounds 2,618 could be staked at 2-1, with over pounds 1,000 more of the same on Betdaq and Sporting Options. Even after taking commission into account, that represents a healthy premium on the Big Three's prices.

Beef Or Salmon, a best-priced 4-1 with Ladbrokes, was available at 4.7-1 with Betfair. Almost pounds 7,000 could be staked at 9-2 or above; still better, post-commission, than Ladbrokes, and markedly better than Hills and Coral's 7-2.

In the Champion Hurdle, Ladbrokes offer a best-priced 9-4 against Rhinestone Cowboy (as low as 7-4 with Coral).

A Betfair customer could have over pounds 800 at 5-2, with almost pounds 4,500

to be staked at 2.4-1 or above - marginally better, at the top rate of commission, than Ladbrokes.

The betting percentages on Betfair are eyebrow-raising. With 37 horses quoted for the Gold Cup, they are betting to just 112 per cent. Ladbrokes quote 28 horses, and are betting to 163 per cent.

The top ten in Betfair's market represent only about 93 per cent, a figure it is hard to believe can be sustained. This compares with 120 per cent for the top ten in Ladbrokes' book.

In the Champion Hurdle, with 33 horses quoted, Betfair's book represents just 108 per cent, while the 22 quoted by Ladbrokes represent 142 per cent.

The top ten in Betfair's market take out about 92 per cent, compared with about 109 per cent for Ladbrokes.

On many horses, only small sums can be staked on the exchanges, but it will be interesting to see how the prices move as the Festival approaches.