

STATE OF NEW YORK
OFFICE OF THE INSPECTOR GENERAL

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REPORT TO THE GOVERNOR
ON THE INTEGRITY OF THOSE
SEEKING TO OPERATE THE
RACETRACKS AT AQUEDUCT,
BELMONT PARK AND SARATOGA

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INTRODUCTION

The Office of the New York State Inspector General has been charged by Governor Eliot Spitzer with conducting a due diligence review of the ethics and integrity of the entities seeking to obtain the franchise to conduct thoroughbred horse race meetings at New York State's Belmont Park, Aqueduct and Saratoga Racetracks. In carrying out this directive, the Inspector General's Office conducted its analysis independently, consistently, fairly and comprehensively, with a view towards ensuring that the franchise would be operated by a company of the utmost integrity. The findings of this review are herein reported to the Governor.

General Background

Since 1955, the New York State Legislature has awarded to the New York Racing Association (NYRA), previously known as the Greater New York Racing Association, the franchise rights to operate Belmont Park, Aqueduct, and Saratoga racetracks. Today, these franchise rights also include the Legislative authorization for the granting of a license to operate video lottery terminals, or VLTs as they are commonly known, at Aqueduct Racetrack. In the future, these rights could be extended. Under New York State Racing, Pari-Mutuel Wagering and Breeding Law, NYRA's franchise will expire on December 31, 2007. In 2005, then-Governor George Pataki formed the Ad-Hoc Committee on the Future of Racing, which solicited and reviewed proposals from bidders seeking the racing franchise. Ultimately, on February 21, 2007, the Ad-Hoc Committee recommended that Excelsior Racing Associates be granted the franchise. This recommendation was neither binding on the Governor nor the Legislature, with the final

franchise award to be granted through the legislative process. The Legislature did not act on the Ad-Hoc Committee's recommendation.

After taking office, Governor Spitzer pledged to make integrity a prerequisite for any firm seeking to obtain the racing franchise. Rather than follow the recommendation of the Ad-Hoc Committee, in which "integrity and responsibility" was simply one factor, comprising 20 percent of the final decision, Governor Spitzer, on February 28, 2007, formed a new panel (Franchise Review Panel) headed by Richard Rifkin, Special Counsel to the Governor, to solicit and review new bids for the management of the thoroughbred racetracks and associated VLTs. In the panel's review, integrity would be a prerequisite to being considered for the franchise award, rather than just one of several factors to be weighed together.

In early March 2007, the Governor's Office requested that the Office of the Inspector General assist the panel by reviewing the integrity of the companies that had identified themselves as bidders. Anticipating that the Legislature might select a bidder by the scheduled end of its session on June 21, 2007, the Governor requested that the integrity reviews be completed by early May. Given the time available for this important process, the Governor's Office and the Office of the Inspector General agreed to seek outside assistance to help gather the information required for the integrity reviews. Criminal history checks would be performed with the assistance of the New York State Division of Criminal Justice Services (DCJS) and the Federal Bureau of Investigation (FBI), and the New York State Police would provide investigative assistance regarding the subjects' prior regulatory histories with gaming and licensing authorities. In addition, each bidder would be required, at its own expense, to engage directly with a private

consulting/investigative firm that would perform the essential research for the integrity review. Upon completion, the private firms would furnish their reports to the Office of the Inspector General which, after its own review and analysis, would present its report to the Franchise Review Panel.¹

Engagement of Consulting Firms

On March 12, 2007, the Office of the Inspector General contacted eight prominent consulting and investigative firms, inviting them to present proposals for conducting the research required for the integrity reviews. Each firm was asked to prepare a proposal, including the resumes of staff to be assigned to the project, a sample integrity questionnaire, and a sample report. Four firms responded to the invitation.

The four made presentations on March 14 or March 15. During the presentations, in which the firms' representatives discussed the extensive work they intended to undertake, it became clear that no one firm could conduct the integrity reviews of all six potential bidders in the time allotted. The Office of the Inspector General thus determined that more than one consulting firm would be retained. Ultimately, the Office of the Inspector General selected three firms based on, among other things, relevant experience; availability of qualified staff; ability to perform the required tasks comprehensively; demonstration of an understanding of the project and a realistic assessment of the workforce required to complete the necessary work; willingness to

¹ Early on in the process, the State Inspector General, Kristine Hamann, learned that a law firm with which a member of her family was associated represented one of the bidders in the franchise award process. While the family member had no involvement with either the bidders or with the process in general, the Inspector General recused herself from continued involvement in this integrity review.

work collaboratively with other consulting firms; and the quality and relevance of sample questionnaires and reports.

Initially, each firm was asked to conduct integrity reviews for two bidders. After ensuring that there would be no conflicts of interest, such as a firm examining a bidder with which it had a pre-existing business relationship, the Office of the Inspector General assigned bidders to the consulting firms balancing their respective workloads. Deloitte Financial Advisory Services was assigned Excelsior Racing Associates and the New York Racing Association (NYRA). PricewaterhouseCoopers was assigned Capital Play, Ltd. and Thoroughbred Racing-NY. Thacher Associates was assigned Empire Racing Associates and Catskill Off-Track Betting Corporation. Before the work could begin, Thoroughbred Racing-NY withdrew. Catskill Off-Track Betting failed to engage the assigned firm to conduct the required research for the integrity review, and was therefore disqualified as a bidder.

Once the integrity reviews were underway, the investors and managers of the bidding companies began and continued to shift. In a number of cases, these changes were a direct response to the requirement of participation in the integrity review process. As a result of the various adjustments, new conflicts of interest emerged and the workload among the consulting firms became unbalanced. To avoid conflicts of interest and to complete the work in a timely fashion, responsibility for investigating certain individuals or entities was reassigned among the three firms as the project progressed.

Scope of Report

The following report represents an integrity review of the bidders for the franchise rights to operate Aqueduct, Belmont Park, and Saratoga thoroughbred racetracks and any associated VLTs. Neither the consulting firms, nor the Office of the Inspector General, have analyzed the capacity of any of the bidders to meet its financial or operational obligations if selected as the franchisee. This report presents no assessment of the financial viability and sustainability of any of the proposed bidders, nor does it assess any bidder's capability to manage the franchise or operate the specified facilities. Except for criminal history and licensing information gathered by the FBI, DCJS, and the State Police, the information contained herein was collected by the consulting firms, and has not been independently verified by the Inspector General's Office.

Methodology

In conducting the integrity reviews, a primary priority of the Office of the Inspector General was to ensure that bidders were treated uniformly throughout the process. To this end, the Office of the Inspector General took every step to ensure that the consulting firms followed the same procedures in conducting their work. These steps included:

- Drafting a uniform letter of engagement between the bidder and consulting firm;
- Agreeing upon a uniform fee structure and billing procedure to be used by each consulting firm;²

² Where bidders or associated entities did not engage the consultants until late in the process, the consulting firm was permitted to establish a more frequent billing schedule.

- Drafting identical questionnaires to be distributed to all participants in the bidding process;
- Ensuring that each consulting firm had identical criteria for determining the most appropriate level of scrutiny for each level of participant in the process, while allowing the flexibility to further research potential concerns where they arose;
- Sharing communications regarding the questionnaires between the Office of the Inspector General and individual bidders with all other bidders; and
- Developing a report outline that all three consulting firms would utilize in presenting their final reports to the Office of the Inspector General.

Due to the major financial investments required of the bidding firms, and the multifaceted operational requirements involved in assuming the racing franchise, all of the bidders except for NYRA consisted of multiple investors, lenders, and managers. Except for NYRA, each of the bidders was a newly organized company. NYRA, a non-profit entity and the current franchise holder, has a well-defined, pre-existing corporate structure and has not committed a large up-front investment in its bid to retain the franchise. Consequently, for three of the four bidders, the integrity review consisted not only of an examination of the bidding company itself, but also consisted of the identification and examination of parent companies and affiliated individuals and entities.

The integrity review covered all members of the bidding companies, including all investors and persons in positions of responsibility within each company. Certain members were further identified as subjects for additional research.

- A “key person” was defined as a principal, director, or officer of the bidding company; an individual holding at least 2.5 percent of the bidding company’s issued and outstanding units; an individual who participates in overall policy-making or financial decisions for the company; a person in a position to control and direct the company’s overall operations; an authorized signatory to bank accounts and debt instruments; or a non-voting unit holder.
- In addition to the bidding company, a “business entity” included any company with at least a 2.5 percent interest in the bidding company; that participates in policy-making or financial decisions; or that will control and direct the operations of the bidding company.
- A “person of interest” included any individual or company formerly in a position of responsibility with the bidding company, or who sold all or part of his or its interest in the bidding company so as to avoid being identified as a key person or business entity.

In the case of NYRA, certain persons with managerial responsibility, although defined as “key persons” under the above definition, were subject to research that was somewhat more limited in scope, as these individuals had previously been subject to intensive evaluation during the period March 1, 2004 to July 24, 2005, when NYRA was subject to the oversight of a court-appointed monitor.

The Office of the Inspector General identified the following topics for the integrity review: business affiliations; criminal histories; involvement in civil litigation; regulatory licenses and findings or actions of regulatory agencies; political contributions

and lobbying; judgments, liens, and bankruptcies; and any media reports that might reflect negatively on the bidding company.

The majority of the information in the above categories was gathered from electronic records. Electronic database searches of public records are necessarily limited to those jurisdictions where records are available on-line. In some instances, manual searches of public records were conducted in jurisdictions deemed likely to possess records of a particular person or entity, such as the jurisdiction of an individual's residence or a business's incorporation. Despite these efforts, this report, in some instances, contains information such as court filings or business affiliations where pertinent records are only available for manual search in the county in question.

Databases were searched to identify lawsuits, business affiliations, and financial histories including bankruptcy records related to the subjects in United States District and Bankruptcy Courts nationwide; litigation, liens, judgments, and UCC filings in all counties nationwide whose records are available on-line; Secretary of State records, limited partnership filings, fictitious business name (DBA) filings and media sources to identify businesses with which the subjects currently or formerly have been affiliated as officers or directors, as well as affiliates or subsidiaries, as applicable.

Regulatory searches were conducted by accessing on-line files containing disciplinary actions and sanctions collected from various federal and state agencies such as the National Association of Securities Dealers (NASD), the Securities and Exchange Commission (SEC), and other federal and state agencies. The U.S. Department of the Treasury's Office of Foreign Assets Control master list of Specially Designated Nationals

and Blocked Persons/Entities, and other databases related to U.S. and international security risks were also searched. In addition, the consulting firms reviewed regulatory filings on each key person provided to them by the New York State Police, which assisted by contacting regulatory agencies throughout the United States.

In all, tens of thousands of documents were reviewed. Record searches extended throughout the United States, and to Canada, Ireland, and Australia.

Database searches were also used to identify any publicly-available information that might reflect negatively on a person's or entity's reputation, or on the reputation of a bidding company. In addition to the sources listed above, the search for adverse references to subjects included a nationwide review of on-line media from numerous sources including newspapers, magazines, trade and industry journals, broadcast transcripts, and wire services.

Key persons were asked to request a personal criminal history record review from the FBI. These reviews, conducted pursuant to 28 CFR § 16.30-16.34, were conducted with the assistance of DCJS. Utilizing the names and addresses furnished by the bidding companies, the Inspector General's Office requested that DCJS forward fingerprint packets to the specified key persons. The packets included two copies of the fingerprint form to be used by the individual's local law enforcement agency to record the fingerprints, together with a cover letter from the Inspector General which provided instructions for the fingerprinting procedure. Also enclosed was a second cover letter which was to be completed, signed and returned together with the fingerprint forms to the FBI. At the completion of the process, the aforementioned documents, including the

results of the FBI's criminal history check, were to be returned to DCJS, which in turn informed the Inspector General's Office of any criminal history information obtained.

In addition, all key persons and business entities were asked to complete, and attest to, questionnaires. The questionnaires included requests for detailed information regarding business affiliations, financial status, political affiliations, and other integrity-related issues. Key persons were also asked to sign waivers authorizing release of personal information by third parties. The questionnaires and accompanying documentation (such as tax returns and corporate financial statements) were examined and compared to publicly-available records to identify any inconsistencies or omissions. Where practicable, key persons and other individuals were interviewed to obtain additional information and to attempt to resolve any inconsistencies or omissions identified in the questionnaires. Where appropriate and, again, practicable, persons of interest were interviewed regarding their withdrawals or divestitures of interest in the bidding company.

The consulting firms ultimately provided hundreds of pages of detail produced during the above-described information-gathering process, with items of potential concern, however minor, reported. The Office of the Inspector General, after reviewing the consultants' reports, has set forth below a summary of potential integrity concerns, as well as information from the consultants' reports deemed relevant for consideration by the Franchise Review Panel. Besides essential background information, this report relates only potential integrity-related concerns.

As a result of both temporal and logistical realities, certain detail regarding potentially-negative information, such as lawsuits or liens could not, in some cases, be ascertained. In addition, certain discrepancies between questionnaire answers and other records could not be reconciled. Although these discrepancies may have legitimate explanations, such as an innocent omission in a questionnaire, they are nonetheless included in the report below.

Moreover, NYRA, which was under bankruptcy protection, did not receive the court's permission to retain Deloitte Financial Advisory Services to conduct the required integrity reviews until April 3, 2007. Entities or individuals delayed in answering questionnaires; questionnaires were submitted either incomplete or without required notarization; individuals did not submit fingerprints required for criminal background checks in a timely manner; interviews were difficult to secure, sometimes due to the key person's presence outside the United States; and new participants continued to join the process. The report will note those instances in which integrity evaluations could not be completed because of the late entry or non-cooperation of participants.

Following this introduction, an overview of general areas of concern identifies potential integrity issues common to several or all of the bidding entities. Following that, a section is devoted to each bidding entity, with relevant integrity concerns grouped within the individual bidder's section by topic (such as criminal history, regulatory actions, etc.) Only negative integrity-related findings will be discussed. In order to protect the privacy of individuals participating in this integrity process, the Office of the Inspector General has, in some instances, omitted the names of individuals when referring to certain matters that are not of public record.

This report covers, as completely as possible, the individuals and entities involved in the bidding entities as of the date of its issuance. The composition of the bidding entities may well change subsequent to the issuance of this report to the Governor's panel. For example, the large equity investor in Capital Play is likely to syndicate its shares if the bid is awarded to that company, bringing in multiple new investors with equity interests in the company. This circumstance may well occur with other bidding entities as well. In addition, individuals or entities that divested their interest in the bidding company to avoid detailed integrity analysis may re-appear as participants at some time in the future. The Office of the Inspector General recommends that additional integrity reviews be conducted of key persons and business entities appearing after the issuance of this report.

GENERAL AREAS OF CONCERN

Within the comprehensive list of integrity-related topics that were researched for this report, certain concerns have surfaced across the entire pool of bidders. Of particular note is the involvement of all four bidders, to varying degrees, with companies that facilitate bets from other states or nations. Some of these are companies known as “rebate shops” which, due to low overhead, are able to provide rebates or rewards to high-volume bettors. Rebate shops have, for a significant period of time, been associated with illegal activities such as race-fixing, money laundering, and tax evasion. Since nearly every U.S. racetrack has contracts giving rebate shops access to its pari-mutuel betting pool, most members of the bidding entities already involved in horseracing have some connection to rebate shops. The section below explains the complex issues surrounding rebate shops and reviews other areas relevant to each of the bidding entities, including criminal activity, political contributions or relationships, and civil litigation.

Rebate Shops

All four entities seeking the franchise to operate Aqueduct, Belmont and Saratoga racetracks have ties in varying degrees to rebate shops. A rebate shop is generally defined as an offshore or Indian-reservation-based gambling enterprise that provides customers with refunds, or rebates, on every dollar wagered on a race. The majority of bets placed by customers with rebate shops are placed either via telephone or the Internet. While rebate shops are not, per se, illegal, there is a wide disparity of opinion among racing industry and law enforcement experts as to their importance to and impact on the continued viability of the racing industry.

To understand how a rebate shop operates, one must first understand the fundamentals of pari-mutuel wagering. Simply stated, pari-mutuel wagering is a system in which individuals bet against one another (the total amount bet is called the “handle”), and the racetrack receives a percentage (or “takeout”) of the pool of money wagered. It is distinguished from most casino gambling, where the bettor is wagering against the casino, or “house” as it is commonly called.

Live broadcasts of races on a closed-circuit television (i.e., “simulcasting”) from racetracks and remote access to the pari-mutuel pool have allowed the development of off-track betting (OTB) operations. As these operations have low overhead, they can generate a profit while offering “rebates” to bettors based on the total amount bet. For example, after paying three percent for the simulcast signal, the OTB operators would receive 17 percent of the bets they accepted. If they offered a ten percent rebate to a gambler who might bet millions of dollars each year, the OTB would retain seven percent for itself. The racetracks receive only their three percent simulcast fees, rather than the full 20 percent they receive for bets placed at the tracks. The rebate shop provides the bettor with a valuable service and, according to some experts, has increased profits for racetracks. According to a 2004 government report, nearly \$1.5 billion is wagered each year on U.S. races through rebate shops.

According to experts, even the most skilled horseplayers cannot make a profit at the track over a sustained period of time, not because they cannot pick the right horses, but because they cannot beat the track’s takeout. For instance, if a bettor loses eight percent of all the dollars he bets at the track’s windows in one year, he is still doing much better than the average bettor. With a rebate from a rebate shop, the bettor receives back

a portion of every bet, decreasing potential losses. When combined with specialized computer programs that help savvy bettors to maximize their probability of winning, rebates put these bettors significantly ahead of those betting at the track, and as a result of this decreased risk of loss, rebate shop customers will bet significantly higher sums. One expert who studied rebates for the National Thoroughbred Racing Association Players' Panel has indicated that among certain gamblers, annual wagering has increased tenfold, from \$3 million to \$30 million per year. Predictably, tracks are disinclined to turn away business of this magnitude.

There are, however, serious risks associated with rebate shops. A foreign bookmaking operation is in a unique position to launder illicit drug proceeds through back-door access to pari-mutuel pools in the United States. By betting consistently on races where the risk of loss is known to be relatively slight, money can easily be laundered through the unregulated settlement process by which race tracks and international rebate shops settle pari-mutuel winnings and losses, usually on a monthly basis. For example, by using sophisticated computer arbitrage systems that maximize the probability of selecting winning betting combinations; by "batch betting," in which a computer is configured to emulate a betting terminal and in which batches of wagers are transmitted to the totalisator³ at a rate of up to 50 bets per second at the very end of the

³ A totalisator, or "tote," consists of a network of computers and wagering terminals linked by modems and a frame-relay system, which electronically combines wagers into "pools." Based on pool totals, the totes record and display changes in betting patterns and recalculate pari-mutuel odds and projected payoffs in timed intervals. Odds are established based on the proportion of money wagered into the pool on each horse. Odds change throughout the course of the wagering cycle and become final when the wagering pool is closed at the start of a race. When the results of the race are official, the tote calculates the payoffs on all winning wagers.

betting cycle, or in some cases, illegally placed after the cycle is closed; or by simply betting on fixed races, a money-laundering operation can extract “clean” pari-mutuel wagering dollars from a U.S. track, either directly or by using a settlement agent in the United States.

A racetrack can minimize this risk by entering into agreements with only licensed, regulated simulcasting services. Yet even these companies may present integrity concerns. For example, Grupo Caliente is a simulcasting service and licensed bookmaking operation based in Tijuana, Baja, Mexico, that has been the subject of numerous allegations of illegal activities. It manages racetracks and bingo halls in Mexico and has a network of more than 165 off-track betting sites located throughout Mexico and Latin America. In addition, the company has been issued 88 additional permits to operate off-track betting sites and bingo halls in Mexico. Through Grupo Caliente’s race track in Tijuana, Mexico, the company provides simulcasting of races from the United States as well as Mexico. It is licensed by the Mexican Department of Interior, with a license valid for 25 years.

According to various publicly-available sources, including the *Washington Post*, for several years, Jorge Hank Rhon, Grupo Caliente’s chief operator and the current mayor of Tijuana, has been suspected by U.S. law enforcement and Mexican authorities of illegal money-laundering activities related to illicit drug trafficking, particularly with the Arellano Felix drug cartel based in Tijuana.

If a licensed bookmaker such as Grupo Caliente sought to be involved in money laundering, it could easily exploit its status as a licensed bookmaker to launder illicit

proceeds through U.S. tracks' pari-mutuel wagering pools. It is a relatively simple matter for a licensed out-of-country bookmaker to partner with an offshore rebate shop with access to pari-mutuel pools in the United States. Using the anonymity provided by the offshore rebate shops, bookmakers can access the pari-mutuel wagering pool to control risk by "laying off" significant wagering activity to one of the offshore rebate shops permitted to place bets into U.S. tracks' pari-mutuel pools.

At least two gaming regulators have formally made known their concerns about Grupo Caliente, Jorge Hank Rhon and a Grupo Caliente associate. The Nevada Gaming Control Board (NGCB), perhaps the preeminent gaming regulator in the country, has cited Grupo Caliente in three different public hearings relative to the licensing suitability of American Wagering in June 1997, as well as in connection with VirtGame Corp. in October 2002. Essentially, these companies were directed by the NGCB to conclude any contracts with Grupo Caliente and to not renew those contracts. Grupo Caliente's U.S. representative for simulcasting events in the United States and Mexico, Arturo Alemany Salazar (who operates a company called MIR International), came under similar scrutiny by the Puerto Rico Racing Administration (PRRA). (The PRRA reviews applications and makes recommendations to the Puerto Rico Racing Board, which reviews the recommendations and renders a final decision whether to grant a license.) Mr. Salazar, of San Diego, California, was a recent applicant for licensure with the PRRA in connection with an application submitted by Codere S.A., a company for which Mr. Alemany was serving as a consultant. During the course of its investigation, the PRRA has received a recommended finding of "unsuitability." Prior to the delivery by the PRRA to the Puerto Rico Racing Board of its formal recommendation regarding Codere and Mr. Alemany,

Codere withdrew its application from the licensure process and upon Codere's withdrawal, Mr. Alemany's application was withdrawn as well. Consequently, Mr. Alemany's application was never the subject of a "formal" recommendation by the PRRA and was never considered by the PRRB.

A federal criminal indictment in the Southern District of New York sheds further light on the nature and extent of the problems associated with offshore rebate shops. In 2005, the United States Attorney for the Southern District of New York announced an 88-count indictment charging 17 defendants with operating an illegal gambling business (*United States v. Uvari, et al.*, Indictment 05 Cr. 24, hereinafter referred to as the *Uvari* Indictment). The charges included conspiracy, money laundering, violations of the Wire Act, extortion, and horse doping. The defendants included Gerald, Cesare and Anthony Uvari, all alleged to be associates of the Gambino organized crime family, who have since pleaded guilty to operating an illegal gambling business. Several of their co-defendants have likewise pleaded guilty, including a former trainer who admitted to fixing a race at Aqueduct in 2003 by administering a performance-enhancing substance to a horse that went on to win its race.

According to the indictment, the *Uvari* illegal-gambling ring served as the middleman between bettors and offshore rebate shops, handling more than \$200 million in bets over a four-year period. The *Uvari* group allegedly concealed the identities of the actual bettors, facilitated tax evasion, and committed fraud by aggregating tax losses to a single Social Security number. The rebate shops named in the indictment were Racing Services, Inc. (based in Fargo, North Dakota), a gambling operation located on the Tonkowa Indian Reservation in Oklahoma, Euro Off-Track (based on the Isle of Man,

United Kingdom), International Racing Group, Inc. (based on Curaçao, Netherlands Antilles), and Elite Turf Club (based on Curaçao, Netherlands Antilles).

After the announcements of the *Uvari* Indictment and a similar indictment in North Dakota,⁴ the New York Racing Association (NYRA) cut off its simulcast signal and terminated its contracts with certain offshore and Indian reservation-based rebate shops. In January 2005, NYRA terminated its simulcast contracts with the following ten rebate shops (often referred to as the “NYRA Ten”):

- Euro Off-Track, based on the Isle of Man in the United Kingdom
- International Racing Group, Inc., based on Curaçao, Netherlands Antilles
- Elite Turf Club, based on Curaçao, Netherlands Antilles
- Tonkawa Indian Reservation, based in Oklahoma
- Racing and Gaming Services, Inc., based on St. Kitts, West Indies
- Lakes Region Greyhound Park, based in New Hampshire
- Capital Sports Ltd., based in Australia
- Darwin All Sports, Ltd., based in Australia
- Coeur d’Alene Casino, based in Idaho
- Excelsior Casino, based on Aruba

Shortly thereafter, on January 27, 2005, the New York State Racing and Wagering Board issued a letter to all New York Racetrack Presidents and General Managers withdrawing its approval of any contracts between New York simulcast licensees and the NYRA Ten. The stated basis for the Racing and Wagering Board’s prohibition was “[t]o maintain the integrity of all New York State Thoroughbred and harness racing and pari-mutuel wagering.” [To the extent that this report contains references to the Board’s January 27, 2005 letter and its consequences, the term “banned” (or similar language) in this context refers only to the Board’s withdrawal of its approval of simulcast contracts.]

New York's Racing and Wagering Board did not, however, prohibit New York tracks from doing business with all rebate shops. In late 2006, the Board authorized two of the previously banned entities, Racing and Gaming Services, Inc. and the Lodge at Belmont (formerly known as Lakes Region Greyhound Park), to again receive simulcast signals from New York racetracks. NYRA also sends its own simulcast signal to known rebate shops such as Lien Gaming and Bettor Racing, reportedly because they are regulated. But regulation alone provides no guarantee. NYRA, for example, continued to do business with Racing Services, Inc., which was regulated by the North Dakota Gaming Commission, until its owner was indicted for tax fraud and other federal offenses.

NYRA seemingly understands the economic necessity of rebates. In a 2005 letter to the Racing and Wagering Board, a NYRA official acknowledged that "the ability to obtain rebates is a major factor in the betting public's decision-making process when determining where to conduct their pari-mutuel wagering activities." In fact, NYRA has recently started its own Rewards Program, giving money back to frequent bettors who reach certain betting-dollar thresholds. This rebate program extends not only to bets placed at the tracks but also to telephone and Internet wagering. NYRA officials project that their new Internet betting program, which started on May 2, 2007, could potentially generate more than \$30 million annually (about 6.5 percent of its total annual handle) and help foster the future economic viability of horseracing in New York State.

⁴ *United States v. Racing Services, Inc., et al.*, Indictment 03-03-112

While rebate shops are not banned under New York State law, there is an on-going debate as to whether there is a federal prohibition. The U.S. Department of Justice has taken the position, as explained in its 2000 letter to the New York Racing and Wagering Board, that the federal Wire Act (18 U.S.C. § 1084) “prohibits the interstate transmission of bets or wagers regardless of the legality of such wagering activity in the sending or receiving state or foreign country.” The Wire Act also, with limited exception, prohibits the transmission of information assisting in the placing of bets or wagers, which can include items such as the line or point spread, bettor names, account numbers, telephone numbers, or information relating to payouts or gambling debts. The Justice Department has concluded that the “placement of wagers by New York residents physically located in New York via account wagering with a wagering entity located outside of New York State may be viewed as involving the interstate transmission of bets or wagers,” and “this activity may well violate Section 1084,” among other federal laws.

Although the conviction in *Racing Services, Inc.* was ultimately overturned by a federal appeals court, the court opined that, “[T]he plain language suggests that Congress intended to prohibit *all* interstate wagering by wire, whether or not legal in states between which the bets are transmitted.” (Emphasis original) “There is explicit support for this interpretation in the legislative history. ... Here, the trial record suggests that North Dakota passed the 2001 account wagering statute in an attempt to attract interstate electronic betting. If the reach of [the Wire Act] is as broad as its legislative history suggests, the attempt if successful will violate federal law. We leave that issue to another day.”

Notwithstanding this court opinion and the Justice Department's position, there is another federal law that legalizes intra- and inter-state account wagering. The Interstate Horseracing Act of 1978 (15 U.S.C. § 3002[3]) was amended in 2000 to expressly authorize account wagering through a definitional change to the term "interstate off-track wager," which is now defined as:

[A] legal wager placed or accepted in one State with respect to the outcome of a horserace taking place in another State and includes pari-mutuel wagers, where lawful in each State involved, placed or transmitted by an individual in one State via telephone or other electronic media and accepted by an off-track betting wagering system in the same or another State, as well as the combination of any pari-mutuel wagering pools.⁵

The apparent contradiction between the provisions of the Interstate Horseracing Act (IHA) and the view of the Justice Department is currently being explored in connection with a formal complaint filed in 2003 by the country of Antigua against the United States with the World Trade Organization (WTO). In its complaint, Antigua has challenged the ability of the United States to enforce certain federal gaming laws (specifically, the Wire Act, the Travel Act and the Illegal Gambling Business Act [collectively referred to herein as the "Acts"]) against foreign companies that accept Internet wagers from U.S. residents. At issue is whether the enforcement of the acts against foreign companies violates the General Agreement on Trade in Services (GATS).

⁵ Eighteen states have expressly enabled account wagering via statute or regulation, including New York State.

In November 2004, a WTO panel ruled that the United States, as a signatory to GATS, could not enforce the Acts against foreign companies that were accepting Internet wagers from U.S. residents. The United States appealed the ruling and in April 2005, the WTO's appellate body ruled that although the U.S. had demonstrated that the Acts were necessary to protect public morals, the U.S. did not enforce the Acts consistently between U.S. companies and foreign companies (as required by GATS). The WTO's appellate body specifically referenced the IHA as being inconsistent with the U.S.'s stated policy against Internet wagering.

The United States argued that the Acts, and specifically the Wire Act, apply equally to domestic companies and foreign companies, and that the IHA does not create an exception for U.S. companies to accept Internet wagering on horseracing. The WTO's appellate body did not rule on whether an exception for U.S. companies was created under the IHA, but recommended that the WTO's Dispute Settlement Body request the United States to bring measures found to be inconsistent with GATS into conformity with its obligations under GATS. The United States was given until April 3, 2006, to bring its policies in line with the ruling.

In April of 2006, the U.S. delegation to the WTO submitted a brief report (the U.S. Report) to the Dispute Settlement Body, stating that no changes were necessary to bring U.S. policies in line with the ruling. In support of its position, the U.S. delegation informed the Dispute Settlement Body that the U.S. Department of Justice recently confirmed the U.S. government position regarding remote wagering on horseracing in testimony before a subcommittee of the U.S. House of Representatives. According to the

U.S. Report, in that testimony, the Department of Justice stated its view that regardless of the IHA, existing criminal statutes prohibit the interstate transmission of bets or wagers, including wagers on horseracing, and informed the subcommittee that it is currently undertaking a civil investigation relating to a potential violation of law regarding this activity.

On January 25, 2007, the WTO compliance panel issued its interim finding in response to the U.S. Report, and found that the United States had failed to comply with previous WTO rulings regarding restrictions on access to the U.S. Internet gaming market. It is anticipated that the United States will appeal this finding. Consequently, the effect of the WTO ruling on the ability of U.S. companies to accept Internet wagers and other account wagers on horseracing is unclear. While the WTO decision does not affect any existing federal or state law, it is uncertain what actions, if any, the U.S. government will take in response to the request of the WTO. One of the options available to is to prohibit or substantially restrict the conduct of interstate simulcast wagering or advance deposit wagering.

It should also be noted that the federal Internet Gambling Prohibition and Enforcement Act of 2006 prohibits those involved in the business of betting or wagering from accepting any financial instrument, electronic or otherwise, for deposit that is intended to be utilized for unlawful Internet gambling. However, the act declares that nothing in the act may be construed to prohibit any activity allowed by the IHA. The act also contains a "Sense of Congress," which explicitly states that it is not intended to criminalize any activity currently permitted by federal law. The U.S. Secretary of the Treasury was directed to promulgate regulations to enforce the provisions of the act and

ensure that the regulations do not prohibit any activity that is excluded from the definition of unlawful Internet gambling, including those activities legal under the IHA.

While the impact of these federal laws is unclear, another debate continues: whether rebate shops are in the interests of the horseracing industry. The focus of this debate is on the economics of the industry. Some track owners and horsemen argue that it is unfair that rebate shops do not contribute their fair share to the tracks and horsemen. They blame rebate shops for the so-called problem of “handle up, purses down,” arguing that rebate shops are most likely diverting pre-existing bettors who formerly bet through tracks or OTBs and, therefore, lower the takeout. The National Thoroughbred Racing Association, or NTRA, claims that while the additional handle from increased bets from high volume bettors at rebate shops may contribute somewhat to track revenue and purses, the effect is mitigated by adverse impacts on effective takeout rates for most other bettors. Gamblers getting rebates ostensibly have a significant competitive advantage over other bettors as they use sophisticated computer programs to analyze races and calculate optimal betting strategies. For this reason, Tampa Bay Downs in Florida, as well as a number of other tracks, reportedly have chosen not to allow rebate shops access to their betting pools.

On the other hand, rebate shop supporters believe that rebates attract high-volume bettors to horseracing, make racing competitive with other forms of gambling, and are examples of free enterprise creativity. They contend that rebates attract legal gambling money that would otherwise not be wagered, thus increasing the handle. The owner of one horseracing consulting firm claims that a ten percent rebate should generate an extra 70 percent in wagering. Another proponent estimates that some bettors wager as much as

ten times their usual amounts at rebate shops. His research also found that there are fewer than 1,000 of these customers and that they are price sensitive, so that without rebates their bets would be substantially less. He further claims that these bettors are responsible for a significant amount of the industry's handle.

While the debate over the economic impact of rebates continues, the attendant integrity concerns remain, and it is within this context that this integrity review examined the relationships of each of the bidding companies with rebate shops.

Criminal Histories

As a fundamental element of this review, 87 key persons were asked to submit fingerprints in order to investigate their criminal histories. As described above, each of these individuals was forwarded a packet with the necessary materials. Key persons were to be fingerprinted at their local police stations and to return the materials to DCJS. Of the 87 packets distributed, 80 have been returned to DCJS and forwarded to the FBI. Fingerprint packets were never received from the following individuals: Becky Thomas and Jeffrey Tucker of Empire Racing; Stephen Wynn of Excelsior; and Richard Santulli, David Smuckler, and Georgette Mosbacher of the New York Racing Association. One key person dropped out of the process subsequent to receiving a packet and did not submit any fingerprints.

Through the submission of these fingerprints, the FBI identified one key person as having a pending criminal case. Two others, who have not yet submitted fingerprint cards, disclosed prior criminal convictions. While the FBI extended an unusual courtesy to the Office of the Inspector General in expediting these reviews, approximately 23 were

still outstanding as of the writing of this report due to delays in returning the fingerprint cards to DCJS. We recommend that the awarding of the franchise be contingent upon the completion of the criminal history review for all key persons of the entity awarded the franchise.

Lawsuits or Regulatory Actions

This integrity review revealed numerous civil lawsuits involving key persons or business entities of all bidders. Many of these actions are of the type to be expected in the normal course of business and do not necessarily reflect negatively on the integrity of the involved parties. Accordingly, this report will list only those matters that may bear on the integrity of the bidder or that were not disclosed in questionnaires.

Political Relationships or Contributions

While there is nothing illegal in making contributions to political candidates, or having personal or business relationships with political officeholders, these areas were nonetheless examined to identify any appearance of impropriety in the awarding of the franchise. Numerous individuals associated with bidding entities either have relationships with, or have made sizable contributions to, political leaders in New York State, including the Governor and the Senate Majority Leader, both of who will play a major role in the selection of the franchisee. In addition, most of the bidders have employed lobbyists as part of their efforts to secure the franchise. Only significant contributions or lobbying efforts will be discussed below.

NEW YORK RACING ASSOCIATION

The New York Racing Association (NYRA), organized in 1955, is a not-for-profit association franchised by New York State to conduct racing and pari-mutuel betting at New York's three major thoroughbred race tracks, Aqueduct, Belmont and Saratoga. In return for its exclusive franchise, NYRA is required to provide the state with certain revenue in the form of pari-mutuel taxes and an annual franchise fee. Unless extended by the Legislature, NYRA's franchise will expire on December 31, 2007.

Recent History of NYRA

In December 2003, an indictment was filed in the federal District Court of the Eastern District of New York, which charged NYRA with one count of Conspiracy to Defraud the United States in violation of Title 18, United States Code, Section 371, and three counts of Aiding and Abetting False Tax Filings in violation of Title 25, United States Code, Section 7206(2). These charges alleged that NYRA had engaged in accounting and reporting practices which enabled its pari-mutuel tellers to engage in systematic tax evasion. Various employees of NYRA who had worked in its Pari-Mutuel Department were also charged with crimes in that same indictment.

NYRA entered into a Deferred Prosecution Agreement (DPA) and a Stipulation of Facts with the United States Attorney's Office for the Eastern District of New York (USAO) on December 10, 2003. Through the DPA and the Stipulation of Facts, NYRA admitted to, and accepted responsibility for, the crimes charged against it in the indictment. As a result of entering into the DPA, NYRA was given the opportunity to avoid a criminal conviction by complying with the conditions set forth in the agreement.

The DPA also provided for the appointment by the Court of an independent monitor to, among other things, monitor NYRA's compliance with the terms of the DPA.

The law firm of Getnick and Getnick was appointed as Monitor of NYRA on March 1, 2004, by the Honorable Arthur D. Spatt, United States District Judge for the Eastern District of New York. Judge Spatt's order set forth the duties and responsibilities of the monitor and gave Getnick and Getnick broad authority to monitor NYRA's business operations to ensure that NYRA complied fully with all federal, state and local laws and regulations. The monitor was also directed to suggest structural reforms that would help ensure NYRA's continuing compliance after the monitor's term expired on July 24, 2005. On September 13, 2005, the Monitor submitted both a final public report which addressed NYRA's compliance with the DPA, as well as a separate sealed report. The USAO moved to dismiss the indictment, and the court granted the motion.

In addition to the underlying criminal activity, a more complete picture of NYRA's organizational dysfunction had been revealed by two State government reports published in 2003, one by the New York State Comptroller's Office in September, and the other by the New York State Attorney General's Office in June. The State Comptroller's report was entitled "The Case for Reform," and recommended "that NYRA voluntarily accept the imposition of an Independent Private Sector Inspector General (IPSIG) to reform its operating practices, policies and procedures." Getnick and Getnick in fact took an IPSIG-style approach to its monitorship, at the conclusion of which, it determined that NYRA had fully complied with the DPA and the law, and that NYRA had, in fact, reformed itself.

According to the monitor's final public report, the following is a list of the most significant improvements implemented by NYRA during the term of the monitorship, and which the monitor believed should be continued regardless of which organization might be granted the franchise in the future:

1. A safe, healthy and humane environment in which to work and live for the backstretch employees and their families.
2. A refusal to send the simulcast signal to rebate shop betting locations that do not provide full and complete information to satisfy New York State that they are operating in a lawful manner.
3. A strict drug testing program with severe sanctions for violators to guarantee that all races at Aqueduct, Belmont and Saratoga are fairly run and to ensure that bettors are not disadvantaged.
4. Pre-race monitoring barns at each track to prevent the drugging of horses.
5. A fully-funded segregated trust account for the horsemen's funds, together with full access by the horsemen to account records for review and inspection.
6. A comprehensive code of ethics that applies to all track employees, officers and board members, and that is enforced in a meaningful and effective manner.
7. Audited financial statements filed on a yearly basis that are transparent; accurately portray the financial condition of the company; are prepared according to generally accepted accounting principles; and are made available to the appropriate State regulatory agencies for review and inspection.
8. Registration as a Money Services Business, including the continuation of all related reporting requirements, anti-money laundering policies and other financial system

protections that have been implemented by NYRA to meet its obligations to those who have entrusted the track with their funds, and to prevent the facilitation of criminal activity, e.g., money laundering, tax evasion, etc.

The monitor stated, however, that this list is not exhaustive, and that improvements could still be made to those systems which had already been put in place.

Given NYRA's recent history, as highlighted above, in conducting this integrity review it was necessary to ascertain the organizational and behavioral changes which were instituted subsequent to the commencement of the criminal prosecution and during the period of the monitorship, as well as any issues which have arisen subsequent to the monitorship. During the course of its investigation, representatives of the Office of the Inspector General and the consultants met with Neil V. Getnick, Esq., of Getnick and Getnick, the former monitor, to better understand the issues existing today regarding thoroughbred racing in general in the State of New York, in addition to those relating specifically to NYRA itself.

NYRA's Post-Indictment Management Changes

According to the monitor, as required by the DPA, NYRA completed the restructuring of its senior management, as well as its pari-mutuel, legal, security, internal audit, accounting and human resources departments by the end of the first quarter of 2004. NYRA hired Charles Hayward as its President and CEO, and created a new Office of the Chairman. This Office consists of two Co-Chief Operating Officers whose responsibilities include supervision of all business areas and departments of NYRA. C. Steven Duncker and Peter Karches were elected as Co-Chairmen of NYRA's Board of

Trustees and both have served without compensation in their positions. The monitor stated that he had worked closely with both Duncker and Karches during the course of the monitorship and that each had acted with integrity.

Of particular note, as stated in the Monitor's final public report, is the role that Mr. Karches played in NYRA's self disclosure of information bearing on racing integrity to the State Attorney General. That disclosure led the State Attorney General's Organized Crime Task Force (OCTF) to begin an investigation into certain suspicious activity, culminating with the execution of search warrants by the State Police and OCTF investigators at NYRA's three racetracks. As Mr. Karches said at the time:

The New York Racing Association is 100 percent committed to ensuring that nothing is permitted to interfere with the integrity of the races we conduct. The NYRA Trustees and NYRA's senior management want it to be perfectly clear, both to the general public and to the people who are involved in NYRA's racing operations, that we have zero tolerance for anyone who fails to abide completely by the rules of racing. If we see something suspicious occurring at one of our racetracks, the appropriate law enforcement agencies will be immediately notified. If actual wrongdoing is uncovered, the perpetrators will be prosecuted to the fullest extent of the law.

The monitor had also noted that previously, NYRA's relationship with the State Attorney General was seen as being defined by the State Attorney General's June 2003 report which concluded that "crime was part of the culture at NYRA" and characterized NYRA as "an insular, opaque, and unaccountable organization." In contrast is the tenor of the press release issued by the State Attorney General's Office on September 21, 2005, to announce the indictment of two key track officials at NYRA for their roles in a scheme to falsely report the weight of jockeys participating in thoroughbred races at NYRA tracks. The press release stated that the investigation had begun when NYRA trustees, in

a newly formed oversight committee, informed the Attorney General's Office of suspicious activity involving the Clerk of the Scales. The release also stated: "Indeed, had it not been for the reforms put into place by the federal monitor ... [there is] little doubt the old NYRA management would have never even brought their suspicions forward to the Attorney General. The new NYRA management did so immediately, and they should be commended as well."

NYRA's Anti-Drugging Efforts

Likewise, Mr. Karches is credited by the monitor with taking an early lead in encouraging NYRA to combat the drugging of horses. In response to a growing concern about the use of performance enhancing drugs in the horse racing industry, during the span of the monitorship, NYRA instituted several new policies in an effort to combat illegal drug use. Two of the most notable policies are (1) the requirement that all competing horses report to a pre-race monitoring barn; and (2) the requirement that selected horses undergo state-of-the-art pre-race testing for evidence of unauthorized medications or authorized medications administered in an unauthorized amount or manner. NYRA's anti-drugging efforts were not only designed to maintain and improve the public's confidence in the integrity of horse racing in New York, but also to level the playing field for bettors and horsemen alike.

NYRA's Response to Prosecutions Involving Rebate Shops

The *Uvari* Indictment, discussed above, unveiled activities involving horse drugging in a NYRA race by a trainer based at Belmont and illegal betting activity at an illegal rebate shop, as well as the connection between the two. In response, NYRA quickly cut off its contractual arrangements with and simulcast signal to all identifiable

rebate shops. As mentioned above, on or about January 18, 2005, NYRA terminated its simulcast contracts with ten rebate shops.

“To maintain the integrity of all New York State thoroughbred and harness racing and pari-mutuel wagering,” on January 27, 2005, the New York State Racing and Wagering Board issued a letter to all New York racetrack presidents and general managers withdrawing its approval of any contracts between New York simulcast licensees and specifically mentioned the above ten rebate shops with which NYRA had terminated its simulcast contracts.⁶ Within days, NYRA submitted to Racing and Wagering a detailed account of its racing integrity program. NYRA noted the following steps that it had taken in the weeks following the *Uvari* Indictment:

- Terminated its simulcast agreements with the four simulcast outlets named in the indictment;
- Suspended the privileges of a trainer named as a defendant in the indictment;
- Terminated its simulcast agreements with six additional simulcast outlets operating offshore or in Indian territory, citing the need for further assurances of the integrity and transparency of those entities;

⁶ In late 2006, Racing and Wagering authorized two of the banned entities, Racing and Gaming Services, Inc. and the Lodge at Belmont (formerly known as Lakes Region Greyhound Park) to again receive simulcast signals from New York racetracks.

- Continued work with the Racing and Wagering Board and Cornell University to develop testing standards for “milk-shaking”⁷ tests to be implemented in February 2005; and
- Committed, with the Racing and Wagering Board, to implement pre- and post-race testing for milk-shaking;
- Reached agreement with Cornell University whereby Cornell would utilize funding from both NYRA and the New York Thoroughbred Horsemen’s Association (NYTHA) to begin freezing and storing urine samples from horses running at NYRA for future testing.

To alleviate the initial economic impact of its decisions, NYRA, in February 2005, proposed a player rewards program (or rebate program) that rewards account-wagering customers with cash rewards based on a percentage of their account wagering activities. As proposed, the rewards would be credited to the players’ accounts. NYRA made this proposal to the Racing and Wagering Board and advised that it sought to team with certain regional OTBs on this project. As it explained in its application, NYRA sought to expand its account wagering customer base “both through the recruitment of new players and through re-patronization of New York residents who have migrated their account wagering activities to out-of-state and offshore account wagering providers.”

NYRA continued:

⁷ “Milk-shaking” refers to the illegal practice of administering alkalizing agents, most commonly baking soda (sodium bicarbonate), combined with other substances such as sugar or other substances, to a horse for the purpose of neutralizing lactic acid build-up, slowing the onset of fatigue and ultimately improving the horse’s performance.

The timing of this request for the New York pari-mutuel industry is crucial. On January 18, 2005, NYRA terminated its simulcast agreements with ten simulcast outlets that NYRA (and its federal monitor) felt were engaging in poor business practices. These simulcast outlets accounted for approximately \$300 million in handle on NYRA races. According to the Thoroughbred Racing Protective Bureau, as much as 50 percent of this handle is attributable to New York State residents who were conducting their account wagering activities through these out-of-state and offshore simulcast outlets.... We believe that the implementation of a competitive Player Rewards Program will enable NYRA and the OTBs to recapture an even larger segment of this handle, which formerly followed through these out-of-state and offshore entities. This will allow NYRA to off-set some of the negative fiscal impact that has resulted from its good-business decision, and it will further aid NYRA and the OTBs to keep a larger portion of the handle wagered by New York residents on NYRA races in New York.

With Racing and Wagering's approval, this program, entitled "NYRA Rewards," began to be offered to NYRA players on May 3, 2006.

Money Services Business Registration and Reporting Requirements

On February 17, 2005, NYRA voluntarily registered as a Money Services Business (MSB) by filing FinCen form 107. By so doing, NYRA subjected itself to certain reporting and recordkeeping requirements, including the filing of: Currency Transaction Reports (CTRs), which must be filed for deposits, withdrawals, exchanges and other transactions in currency of more than \$10,000; Form 8300s, which must be filed by non-financial institutions when they receive currency in excess of \$10,000; Suspicious Activity Reports (SARs), which some MSBs are required to file when the MSB knows, suspects, or has reason to suspect that certain transactions involve funds derived from illegal activity, are designed to evade the law, or serve no apparent lawful business purpose.

Anti-Money Laundering Policy and Program

As an MSB, NYRA is required to develop, implement and maintain an effective anti-money laundering program. On February 17, 2005, NYRA adopted a formal Anti-Money Laundering (AML) Policy and Program. Below is a list of the relevant AML policies and procedures that NYRA has adopted and implemented:

- Appointed an anti-money laundering compliance officer;
- Distributed the anti-money laundering policy to all NYRA employees;
- Retained professional trainers to conduct training for NYRA employees regarding the new procedures, including CTR requirements, Know Your Customer and Due Diligence Procedures, and Reporting Suspicious Activity Procedures;
- Established an effective method of customer identification for all NYRA customer accounts;
- Filed appropriate reports such as SARs and CTRs for cash transactions greater than \$10,000;
- Instructed all employees to promptly report any suspicious activities to the compliance officer;
- Established a comprehensive record creation and retention program that includes all documentation relating to the identity of each NYRA customer and/or NYRA account holder, and all reports and filings required by applicable law;
- Conducts an independent audit/test of NYRA's anti-money laundering procedures and program, at least once per year, to ensure that they comply with all appropriate laws and regulations and operate effectively; and

- Complies fully with any and all properly authorized requests for information made by federal or state law enforcement agencies regarding the identity of any NYRA customer and/or account holder reasonably suspected of violating any AML law or regulation.

Code of Ethics

Over the course of 2005, NYRA, with the guidance of the monitor and the State Comptroller, developed its current Code of Ethics which was passed by the Board of Trustees in August 2005. It addresses a broad range of issues and circumstances, including: compliance with laws, rules, and regulations; conflicts of interests; bribery; patron wagering and anti-money laundering compliance; employee wagering; tips and gratuities; competitive bidding; unlawful discrimination and harassment; workplace safety and health; and political contributions. NYRA has designated an Ethics Compliance Officer and its Code of Ethics sets forth the various methods available for raising an ethics issue. NYRA has also developed an Ethics Committee comprised of the President/Chief Executive Officer, the Senior Vice President/General Counsel, the Senior Vice President/Chief Financial Officer, and the Senior Vice President of Human Resources and Labor Relations.

Bankruptcy

In early November 2006, NYRA announced that it had filed a voluntary petition under Chapter 11 of the United States Bankruptcy Code with the U.S. Bankruptcy Court for the Southern District of New York, citing the failure of the New York State Lottery Division to approve the VLT casino at Aqueduct as forcing the decision.

According to a published report in the *Times Union* (Albany, NY), NYRA listed more than 130 creditors, and debts and assets both at \$153 million, although documents pointed to deeper liabilities. The state is owed nearly \$100 million from loans and interest, including \$13.5 million from Empire State Development, \$6 million from the Lottery Division loaned since last year, and \$76 million NYRA borrowed over many years from the state's Thoroughbred Racing Capital Investment Fund. State taxes of more than \$600,000 are also owed. Other major creditors are Nassau County, owed \$17 million, and the U.S. Pension Benefit Guaranty Corp., owed \$12.3 million. In December, the *Times Union* reported, NYRA was set to pay the final \$1 million installment on a \$3 million fine from the federal government for its role in a tax fraud conspiracy that resulted in convictions of numerous NYRA clerks.

According to a November 2006 report in the *Times Union*, the state planned to ask the U.S. Bankruptcy Court to dismiss the Chapter 11 filing, contending that the private, nonprofit organization has no right to be shielded from \$309 million in creditors. Also in November, according to a published report in the *New York Post*, five years earlier, the state had passed legislation allowing VLT casinos at New York's racetracks. NYRA entered into an agreement with MGM Mirage to build and operate the casino at Aqueduct which, with 4,500 VLTs, would, it was projected, produce \$400 million a year in revenue for education and millions more for the racing industry. Two years later, the grandstand at the track was gutted as the first step in the construction process.

The casino has been in limbo ever since, occasioned in part by NYRA's legal problems, including the monitorship. As of the time of the *Post's* article, the State Lottery Division had yet to approve NYRA's amended agreement with MGM. In late 2005, the

Post reported, NYRA was on the verge of bankruptcy when the state approved a \$30 million loan, to be paid back with future VLT revenues. NYRA received \$11 million of that loan. Just prior to declaring bankruptcy, the state's Racing Oversight Board had agreed to grant the remaining \$19 million in three installments, but that agreement did not include approval of the casino, and NYRA reportedly turned down the offer. In May 2007, the *Times Union* reported that MGM Mirage had withdrawn from the VLT casino project at Aqueduct.

Update on Integrity Issues Addressed in the Monitor's Final Report

NYRA officials interviewed report that they have continued to adhere to the integrity reforms implemented by NYRA during the monitorship.

Elizabeth Bracken, NYRA's Director of Simulcasting, stated that NYRA has a contract with Hipodromo de Agua Caliente, S.A. de C.V. (Grupo Caliente) to sell NYRA's simulcast signal for a flat monthly charge of \$4,125. According to Ms. Bracken, the wagers of Grupo Caliente's bookmaking customers do not enter NYRA's pari-mutuel pool. Instead, Grupo Caliente is only authorized to distribute NYRA's signal to 212 secondary sites in Mexico, Latin America and the Caribbean, where Grupo Caliente conducts licensed bookmaking operations.

Update on Post-Monitorship Events

- In September 2005, at the same time NYRA was being released from a federal monitorship, then-State Comptroller Alan Hevesi warned that the association was not clear of trouble, according to a September 2005 *Associated Press* article. The article said that a sealed report containing further criminal accusations or evidence

for investigation against NYRA was sent to federal prosecutors. “All the bad news may not be out yet,” Hevesi said.

- Draft audits by the Comptroller have been critical of how NYRA accounted for the franchise fees it owed the state. According to a September 2005 article in the *Albany Times Union*, the unsealed audit said NYRA had failed to pay the state more than \$40 million in franchise fees owed between 2000 and 2003, and alleged that NYRA had improperly deducted expenses, including \$7.6 million in interest on state loan payments that it had not been making. A second story in March 2006 said that an unreleased audit showed NYRA “shorted the state at least \$30 million from 2000 to 2003.”
- According to the *Times Union*, in December 2006, NYRA sued the state for failing to approve the VLTs at Aqueduct, stating that “certain state officials” refused to approve NYRA’s contract for a VLT project at Aqueduct without reason. Calling the state’s actions “unconstitutional and unlawful,” the suit claimed the state is losing \$54 million in VLT revenue. It was also reported that in an action filed in its bankruptcy case, NYRA is seeking a declaration that the state’s attempt to take the Aqueduct, Belmont and Saratoga thoroughbred tracks, which NYRA claims it owns, is unconstitutional and unenforceable.
- As reported in October 2006 by the *Times Union*, NYRA awarded no-bid contracts to two media companies, even though racing law requires competitive bids in most instances. NYRA awarded a contract valued at more than \$300,000 to the *New York Post* and another for about \$400,000 to New York Interconnect, a cable TV system that broadcasts downstate and in some markets in neighboring

states. According to NYRA, the contracts were for ads for the Belmont and Aqueduct racing season and, NYRA claimed, it notified the state of the deals under an exemption allowed under law. Racing law requires competitive bids on contracts of more than \$250,000 unless there is an emergency or the contractor offers a unique service. The “sole-source exemption” requires NYRA to notify the state at least 15 days before contracting for such goods or services, whereas in this instance, according to the *Times Union*, NYRA notified the state after the fact.

- NYRA has been subject to two lawsuits filed in U.S. Bankruptcy Court in Manhattan by plaintiffs complaining that it has been improperly diverting money from purses that should go to winning bettors and horse owners. In December 2006, owners and trainers at NYRA tracks sued the association on claims that it had diverted \$15 million to \$20 million from winnings to operating costs. News reports stated that the suit charged NYRA with violating state racing law requiring that a certain percentage of bets go directly into purses. In February 2007, a North Dakota company, Lien Games Racing LLC, sued NYRA for \$1.6 million in bankruptcy court, arguing that NYRA was using money from pari-mutuel pools that should have been earmarked for bettors, according to published reports.
- In early 2006, nearly \$12 million in liens were lodged against NYRA for failing to pay taxes and make payments on two employee pension plans, according to news articles. In February 2006 NYRA received a \$1.13 million tax warrant for failing to pay taxes and penalties on admission charges and bets, according to an

Associated Press article. NYRA President Charles Hayward said the association had told the Governor's Office that in order to keep its finances stable it would not pay its November and December 2005 tax bills. Then, in May 2006, the federal Pension Benefit Guaranty Corp. filed two liens totaling \$7.5 million against NYRA for failing to make payments on two employee pension plans covering 1,100 employees, the *Associated Press* reported.

- An unresolved dispute between NYRA and New York State over who owns the three thoroughbred racetracks overturned a planned attempt at debtor-in-possession financing after NYRA's November 2006 Chapter 11 bankruptcy filing, because it left NYRA without clear title to the real estate to use as collateral, according to a January 2007 story in *TheDeal.com*. NYRA had planned to go to bankruptcy court in January 2007 to ask for approval of \$50 million in DIP financing from GE Capital, the article said.
- The dispute about whether the state or NYRA owned its assets surfaced in another venue as NYRA sought to raise money in December 2005 by auctioning paintings that had been given to it by horse owners, according to *The New York Times*. The state Racing and Wagering Board had threatened a suit, arguing that the state and not NYRA owned the artwork, and so Sotheby's canceled the auction. NYRA had hoped to raise up to \$2 million in proceeds.
- According to a January 2007 article in the *Times Union*, Racing and Wagering Board Chairman Daniel Hogan and Commissioner Michael Hoblock met with representatives of NYRA on January 8, 2007 in what was claimed to be an apparently illegal meeting. Having two of the three commissioners of the board

present represented a quorum, meaning the meeting should have been open, and advance notice given. Neither happened. Chairman Hogan stated that it was unintentional. He said he had planned to meet alone with staff and NYRA, but asked Commissioner Hoblock to join them to clear up some things that happened when Hoblock was chairman. The *Times Union* stated that it was not the first time the issue has come up, as one its reporters had raised it earlier. The discussion included NYRA's application for a simulcast license and its attempts to fire a clubhouse maitre d'. Hogan claimed no action was taken as a result of the meeting.

Key Persons

NYRA submitted 53 Key Person Integrity Questionnaires. In reviewing this information, it became evident that NYRA had designated key persons at a level exceeding that of the other entities seeking the racing franchise, and that NYRA's definition of key persons appeared to exceed the requirements of the questionnaire, especially with regard to operational personnel. In order to maintain as much consistency as possible between the level of inquiry given NYRA and that given to the other entities being reviewed, for the purposes of this inquiry NYRA's key persons were defined to include only the following groups of individuals: all Board Members and Trustees, all shareholders, all officers, and all persons named in the top three levels of NYRA's organizational chart, which was provided in the Business Entity Integrity Questionnaire. This resulted in the designation of 34 key persons for NYRA.

In consultation with the consultants, careful consideration was given to the level of due diligence to be conducted on each key person, based on the unique history of

NYRA. Since NYRA operated under the oversight of the court-appointed monitor until July 24, 2005, during which time all aspects of the entity's operation and personnel were extensively evaluated, it was agreed that those individuals who had been associated with NYRA before or during the monitorship would not be investigated to the same extent as those who became associated with NYRA after the release of the monitor's final report, as they had already been subject to extensive scrutiny. Accordingly, more comprehensive research was conducted with regard to the latter group.

Using the guidelines articulated above, reports were prepared for the following key persons: Dennis Dammerman; Charles Hayward;⁸ Georgette Mosbacher; Barry Ostrager; Leonard Riggio; and John Ryan. Additionally, Key Person Limited Scope Reports were prepared for the following individuals: Chester Broman, Sr.; Paul Campo; Kenneth Cook; Joseph Cornacchia; Michael Del Giudice; C. Steven Duncker; Robert Evans; Albert Fried, Jr.; Lucy Young Hamilton; James P. Heffernan; John A. Hettinger; Stuart S. Janney; Patrick Kehoe; Patrick Mahony; Timothy McGinn; John Meriwether; John Passero; Ogden Mills Phipps; Irene Posio; Michael L. Rankowitz; Richard T. Santulli; Peter G. Schiff; Joseph V. Shields; David Smukler; Stuart Subotnick; John Tierney; William Varvaro; and Charles V. Wait.⁹

⁸ Although Charles Hayward was associated with NYRA prior to the issuance of the monitor's report, he was appointed as a Trustee after the report was issued. Therefore, we chose to conduct a comprehensive background review on him.

⁹ Cathleen Marino and William Nader also appear on the relevant level of the NYRA organizational chart. We were informed by NYRA that Marino was retiring at the end of April 2007, and Nader was leaving the organization. Accordingly, searches were not conducted for these two individuals.

It was also agreed that the consultants would conduct a limited number of interviews to review NYRA's performance with regard to integrity issues identified in the monitor's report dated September 13, 2005. To accomplish this task, the following NYRA officials were interviewed between April 11 and April 13, 2007: Elizabeth Bracken, Director of Simulcasting; Steve Duncker, Chairman; Charles Hayward, President and CEO; Patrick Kehoe, General Counsel; Irene Posio, Chief Financial Officer; and Paul Campo, Racing Secretary.

Discrepancies and Omissions in Responses to Questionnaires

There were various instances of failure to disclose requested information, each varying in significance. Often this failure pertained to undisclosed business entities and litigation. For example, one individual failed to disclose ownership of property. Another failed to identify a relative who is a present or past employee of a racing or gaming entity. Yet another mentioned an employment relationship with a particular company but omitted the fact that he had been ousted from the position. One individual, Richard T. Santulli, failed to disclose a multi-million dollar federal tax lien. Another, Leonard Riggio, failed to provide tax returns with his questionnaire, stating that they would only be made available for review in his presence. Citing concerns about whether the information might eventually be viewed by the public, despite assurances to the contrary, he was the only NYRA key person who failed to provide the requested tax returns.

Legal and Regulatory Issues

In November 1978, the Securities and Exchange Commission ruled that key person Albert Fried, Jr. had artificially inflated the price of common stock of a publicly traded company. In addition to the imposition of a fine, Mr. Fried was suspended from

association with any national securities exchange broker or dealer registered with the SEC for a period of six months (five months of which were commuted) and his membership with a stock exchange was also suspended for the same period. In July 1977, Fried was also fined in another SEC ruling in a matter which alleged that brokers and individuals traded directly with a particular party, giving the party preferential price treatment and failing to disclose the party as a customer in brokerage firm records.

A lawsuit involving two NYRA key persons, Leonard Riggio and Michael Del Giudice, *InterMountain IronWorkers Trust Fund, Derivatively and on Behalf of Barnes and Noble, Inc. vs. Riggio, Barnes and Noble, et al.*, case no. 06-CV-6692, was filed on September 1, 2006 in the U.S. District Court for the Southern District of New York. According to on-line court documents, this is a shareholders' derivative action in which the plaintiffs allege that between 1997 and 2005, the defendants "intentionally backdated or changed the date of company stock options to be granted at a lower price, resulting in defendants diverting hundreds of millions of dollars of corporate assets to themselves through the manipulation of the exercise price of hundreds of thousands of stock options granted to Barnes and Noble insiders." This case is still pending. According to the docket sheet, the following member suits were consolidated with the lead case: 7:06cv6883; 1:06cv6883; and 1:06cv6902. According to SEC filings, the SEC was conducting an informal inquiry into the matter and the U.S. Attorney for the Southern District of New York issued a subpoena for documents regarding the company's options granting practices. An internal investigation by the company found that backdating did occur, but with no intent to defraud, according to SEC filings.

In another lawsuit involving Leonard Riggio, *Dennis C. Vacco, et al., vs. Leonard Riggio, Joseph Carlino, Peter Diamandopoulos, Nicholas Samios, et al.*, case number 40125397, filed on March 24, 1997 in New York County Supreme Court, Dennis Vacco, then New York State Attorney General, alleged that Adelphi University trustees might have had conflicts of interests with the university when they conducted work for the university through their affiliated companies. According to media reports, in 1995 the government began looking into the compensation package of the university president. In 1996, the Board of Regents began a separate investigation, and on February 10, 1997, the Board of Regents ordered the immediate removal of 18 of the 19 trustees, replacing them with new trustees selected by the Regents. While Mr. Riggio was not singled out for any specific wrongdoing, according to on-line filings, he was one of the 18 trustees dismissed.

Multiple lawsuits were filed between August 12, 1991 and July 18, 1994 in the U.S. District Court for the Southern District of New York against key person John W. Meriwether, his former employer Salomon Inc. and others for securities fraud. Eighteen cases were filed in the Southern District of New York against John W. Meriwether, et al. between August 12, 1991 and November 6, 1991. In December 1992, Meriwether was fined \$50,000 and received a three-month suspension by the Securities and Exchange Commission for his role as president of Salomon Inc., for failing to properly supervise employees who rigged bids in the treasury markets.

Judgments, Liens, and Bankruptcies

The following liens and judgments were identified regarding NYRA. With the exception of the first lien, no further information regarding the current status of these liens and judgments was available from on-line records.

- On February 7, 2006, NYRA was the debtor in a \$1.13 million state tax lien. This lien was released on April 19, 2006.
- On January 15, 2006, NYRA was the debtor in a \$2.27 million federal tax lien.
- On January 15, 2006, NYRA was the debtor in a \$1.05 million federal tax lien.
- On October 14, 2005, NYRA was the debtor in a \$2.22 million federal tax lien.
- On August 18, 2005, NYRA was the debtor in a \$1 million judgment issued in favor of the U.S. Attorney's Office for the Eastern District of New York.

On November 18, 1996, a \$3.9 million federal tax lien was filed against Richard T. Santulli by the United States Internal Revenue Service (IRS) in New York County, New York. The lien was satisfied in September 1998. In January 1997, a \$3.8 million federal tax lien was filed against Richard Santulli by the IRS in Eagle County, Colorado. Because of the closeness of dates and amounts, it is possible that the Eagle County Lien is a duplicate of the New York lien.

A \$4,215 tax lien was entered against John W. Meriwether on October 8, 1997 by the New York State Tax Commission. The lien was satisfied on July 1, 1998. Mr. Meriwether said in his questionnaire that he was not the subject of any judgment or lien during the past ten years.

In July 2005, John P. Tierney had a \$552 New York state tax lien filed against him, which has not been satisfied.

The New York State Department of Taxation and Finance filed a \$21,015 tax lien against Steven Duncker on October 4, 2006. This undisclosed lien was satisfied on October 27, 2006.

Political Contributions and Lobbying

As noted previously, various individuals associated with the bidding entities have relationships or have made sizable contributions to political leaders in New York. While the commonality of these activities across the bidding companies prevents any conclusion from being drawn that a particular bidder has gained a particular advantage in this process, the following press accounts are of note.

According to an article in the *Thoroughbred Times* dated December 2, 2003, Kenneth T. Cook made a \$10,000 contribution to Governor George Pataki's campaign prior to Mr. Cook's appointment as security director of NYRA. The contribution came at the same time that NYRA was targeted in a federal investigation regarding its financial practices. An earlier November 27, 2003 *Times Union* article quoted Mr. Cook as denying that the contribution had any impact on his appointment.

Three of Governor George Pataki's appointments to the New York Racing Association, Joseph M. Cornacchia, Chester F. Broman, Sr. and Stuart H. Subotnick, each gave \$25,000 to Pataki's campaign committee shortly before they were selected, according to an October 2000 *Associated Press* article. Each made his donation to Friends of Pataki in July 1998. Pataki appointed Cornacchia two months later and added

Broman and Subotnick to the NYRA board in December of that year. Subotnick had previously given Pataki's campaign \$28,000 in January 1998. It was further reported that the governor's office denied any link between the money and the new trustees, insisting they were chosen because they are successful businessmen and racing enthusiasts.

Stuart Subotnick's 2002 contribution of \$10,000 to Eliot Spitzer's campaign fund was questioned as a potential conflict of interest given the Attorney General's investigation of the chairman of Metromedia Fiber Network, according to a *Forbes* article. (According to SEC filings, Metromedia Fiber Network Services, Inc. was a wholly-owned subsidiary of Metromedia Fiber Network, Inc., which was controlled by Stephen Garofalo, its Chairman and Chief Executive Officer, and John W. Kluge and Stuart Subotnick, who controlled approximately 60 percent of the total voting power of Metromedia Fiber Network, Inc.)

Media Reports

An article in the *Deseret Morning News* dated August 5, 2005 reported that Albert Fried, Jr.'s purchase of a property owned by Geneva Steel was one of several "illicit real estate transactions" made by Geneva CEO Ken C. Johnson. Fried, a creditor of the company as well as a director, purchased a 76-acre property called Williams Farm. In the litigation concerning Geneva Steel's bankruptcy, the trustees of the company alleged that the CEO "violated his duty of loyalty to the debtors by his involvement in third-party real estate transactions" with individuals such as Fried, and "his failure to disclose those actions."

As discussed above, according to *The Wall Street Journal.com* dated April 4, 2007, the SEC conducted an “informal inquiry” into the issue of stock options backdating at Barnes and Noble. According to the company’s 10Q filed the same day, this inquiry came as a result of a derivative complaint filed by a shareholder in New York County Supreme Court on July 6, 2006, alleging improprieties in the company’s issuance of stock options. The complaint named certain current and former executives of the company, including Leonard Riggio, as well as certain members of the Board. On August 28, 2006, the company disclosed that it had received a subpoena from the United States Attorney’s Office for the Southern District of New York requesting documents regarding those stock option practices. According to the *Wall Street Journal*, Barnes and Noble announced that a special panel of its board’s audit committee, along with an independent lawyer, would conduct an internal review of its stock options practices. “On April 4, 2007, the company said the committee found numerous instances of improper backdating but no intent to defraud.”

According to a *Crain’s New York* article dated April 4, 2007, Barnes and Noble Inc. “will take charges related to an investigation into its stock option granting practices, but will not restate financial statements.” According to Barnes and Noble, the review found numerous instances of improperly dated stock option grants between 1996 and 2006. The article stated that “the gross amount of price differences between the former and revised measurement dates over the ten-year period is \$45.5 million, before forfeitures and income taxes. As a result, the company’s Barnes and Noble.com subsidiary will take a charge of \$10 million, and Barnes and Noble will make a \$200,000 adjustment to increase non-cash compensation expense in its fourth quarter which ended

in January.” Barnes and Noble said the charges are not material to its financial statements and therefore no restatements are required. “The company will re-price incorrectly dated and unexercised stock options issued to current officers and directors, other than hiring grants, for a total difference in price of \$2.6 million. Some current officers will pay the company \$2 million, before any netting of allocable income taxes, due to incorrectly dated options.” Barnes and Noble is reportedly one of at least 107 companies to be questioned by federal regulators over the possible backdating of stock-option grants.

According to a *New York Times* article dated February 11, 1997, the New York State Board of Regents issued a report of the results of its investigation into the allegations of misconduct by Adelphi University trustees. The report called for the immediate dismissal of 18 of Adelphi University’s 19 trustees, including Leonard Riggio, stating that the trustees paid the school’s president, Dr. Peter Diamandopoulos, too much and failed to review his job performance. In addition the report accused two ousted trustees of improperly profiting by doing business with university, and of failing to disclose details of their dealings. It further stated that trustees failed to abide by Adelphi bylaws to give faculty a say in how the university is governed. While Riggio was not singled out for a specific allegation of wrongdoing, he was one of the 18 trustees removed.

According to a *Newsday* article dated March 18, 1996, Leonard Riggio, a trustee of Adelphi University, is mentioned in this article which raises the question of whether Adelphi trustees should be allowing the trustees’ firms to do business with the University. The article goes on to state that critics of the University officials also fault the trustees for

inadequate fundraising. While no proof has yet been uncovered showing that Adelphi's "relationships with trustees' businesses have cost the school money, broken laws or violated accepted standards of trustees at private universities," state investigators are reviewing the trustees' business dealings with the school. The New York State Attorney General's Office was "probing Adelphi's President \$532,000 salary and deferred compensation packages and the \$1 million Manhattan condominium apartment the school purchased for the president's use."

An article stated that Heating Oil Partners income trust has lost "more than 90 percent of [its] value since its IPO," which apparently forced it into bankruptcy. The bankruptcy filing occurred while John David Ryan reportedly was the chief operating officer of Heating Oil Partners. Ryan disclosed the bankruptcy in his questionnaire.

In addition, Heating Oil Partners reportedly paid the Environmental Protection Agency a total penalty of \$117,000 for alleged violations of oil spill prevention rules at two oil terminals in Churchville, PA and Philadelphia. The EPA reportedly cited Heating Oil Partners for violating Clean Water Act regulations designed to prevent and control oil spills.

A May 2005 *New York Daily News* article reported that Joseph Cornacchia, Jr. co-owned a race horse with Salvatore Piazza, a reputed mob associate who won state approval to own and run horses in the late 1990's. Mr. Cornacchia told the newspaper that he was a "passive investor" and was "unaware of Piazza's stake in the horse."

Cornacchia owned a number of horses with Edward Swyer, who was one of New York State Senator Joseph Bruno's appointees on the Ad Hoc Committee on the Future

of Racing, a panel reviewing bids for the New York State racing franchise, according to the *Times Union*.

Charles Duncker, a/k/a C. Steven Dunker, owned two horses with the aforementioned Edward Swyer. The horses were sold in 2005 and August 2006, according to the September 2006 *Times Union* article.

According to a January 2007 *The New York Times* article, Timothy McGinn's company, McGinn, Smith and Company, is cooperating with an FBI inquiry and received a grand jury subpoena concerning an investigation into State Senator Joseph Bruno's consulting business. According to the article, in 2001, two of Bruno's campaign committees made loans of \$200,000 to Capital Center Credit Corporation, where McGinn served as chairman. The loans were repaid at interest rates of nine to ten percent and were paid in full in 2004. An article from the website The Albany Project said that the high interest rate loan appeared to have allowed McGinn's company to make campaign contributions greater than New York State campaign finance law allowed. *The New York Times* said that the investments "though legal, were unusual even for New York."

According to on-line profiles, John W. Meriwether spent the 1980s as a partner at Salomon Brothers. In 1991, in the wake of a scandal involving one of his traders, he abruptly resigned. In 1993, Meriwether gathered together his former colleagues and a handful of economists to establish a new hedge fund called Long-Term Capital Management. In 1998, Long-Term Capital Management notoriously collapsed when the firm's staggering \$100 billion balance sheet threatened to drag down markets around the world.

In August 2004, Joseph Shields, his company Shields and Company, and others were required to pay compensatory damages to claimants totaling \$1.2 million in a National Association of Securities Dealers (NASD) arbitration award after a panel ruled that they were “liable for failure to supervise” the purchase and sale of various stocks, including those of America On-line, Intel Corp., Cisco and Lucent Technologies.

In 2002, the SEC opened an investigation into accounting practices at one of Stuart Subotnick’s companies, Metromedia Fiber Network, a provider of high-speed corporate data connections now known as AboveNet. The investigation was not resolved as of January 2005, according to a *New York Times* article.

Beginning sometime in 2000, Subotnick and his business partner, John Kluge, were targeted by institutional investors who questioned their management of Metromedia. Lens Investment Management and Crandon Capital filed lawsuits in 2000 and 2001 respectively, to attempt to force the company to hand over its books to shareholders and alleging that Subotnick and Kluge had purposefully depressed the value of Metromedia’s stock. The Crandon suit alleged that Subotnick and Kluge “intend[ed] to squeeze out Metromedia’s public shareholders to capture for themselves the true value of Metromedia’s communications assets.” At this time, the outcomes of either lawsuit, which were both filed in state court in Delaware, are not known; however, it appears that in March 2001, Metromedia was ordered to turn over its records as a result of the Lens Investment suit, according to an Internet posting on a website monitoring corporate governance issues (corpgov.net).

EMPIRE RACING ASSOCIATES, LLC

Empire Racing Associates, LLC is a limited liability company incorporated in New York State in February 2006 for the express purpose of operating New York racetracks and related gaming businesses pursuant to the anticipated award of the New York racing franchise. Jeffrey Perlee is the Company's Chief Executive Officer; Dennis Brida is Executive Vice President of Racing Operations and Industry Relations; and Justin McDonald is Vice President. Jeffrey Tucker is Chairman of the Board of Managers.

Key Persons and Business Entities

In addition to the executive staff listed above, all members of Empire's Board of Managers were identified as key persons for the purpose of this investigation. The additional members of the Board of Managers are Daniel R. Alonso, Bill Bissett, Bill Cartstanjen, Martin Cunningham, Michael Dubb, Terrance P. Finley, Mark Holliday, Jim Alpine, Ira Raphaelson and Charles Reiss. Board of Managers members Cunningham, Dubb, Finley, Holliday and Reiss also have invested in Empire in amounts ranging from \$25,000 to \$250,000.

Empire's Corporate Statement asserts that the interests of New York's horseracing industry would be best served if the New York racing franchise were owned and operated for profit by a company largely comprised of, and owned by, owners and breeders of New York racehorses. Accordingly, most of the individual members of Empire are horse owners or breeders. In addition to the 38 individual members is the New York Thoroughbred Horseman's Association, Inc., which owns a three percent

interest in Empire, plus six major corporate entities, five of whom are heavily involved in the horseracing and gaming industries. The five racing-related entities collectively own approximately 30 percent of Empire, and are comprised of:

- Magna Entertainment Corp.
- NYRHC, LLC (an affiliate of Churchill Downs, Inc.)
- Delaware North Companies Gaming and Entertainment, Inc.
- Woodbine Entertainment Group
- Scientific Games Holding Corp.

Magna Entertainment Corp (Magna), owning 6.81 percent of the outstanding ownership units issued by Empire, was incorporated in Delaware in 1999 and is publicly traded on the NASDAQ and Toronto Stock Exchanges. Its headquarters is located in Aurora, Ontario. While publicly traded, Mr. Frank Stronach controls approximately 75 percent of the voting shares.¹⁰

NYRHC, LLC/Churchill Downs, Inc. (Churchill Downs), owning 6.81 percent of the outstanding ownership units, was formed in Delaware in August 2006 for the sole purpose of investing in Empire. It is a wholly-owned subsidiary of Churchill Downs, a public corporation traded on the NASDAQ Stock Exchange, its principal business being

¹⁰ According to *The Wall Street Journal* (May 11, 2007), officials of Magna International, Inc., a Canadian auto parts maker, and Oleg Deripaska, a Russian aluminum magnate, announced a plan in which Mr. Deripaska would purchase a \$1.54 billion stake in Magna. United States law enforcement officials suspect Mr. Deripaska of having ties to Russian organized crime. Deripaska's visa to travel to the United States was canceled last year because of Washington's legal concerns. The sale would give Deripaska significant control of Magna, giving him the right to nominate six of Magna's fourteen Board members, the same number as are nominated by the Stronach family that currently controls Magna.

the conducting of pari-mutuel wagering on live horse races, as well as providing simulcasting services.

Delaware North Companies Gaming and Entertainment, Inc. (Delaware North), incorporated in Delaware in January 1980, owns 6.81 percent of the outstanding ownership units issued by Empire. It is a wholly owned subsidiary of Delaware North Companies, Inc., an international holding company which, through its subsidiaries, operates in the hospitality, food service, guest relations and sports, and entertainment management industries. Through Delaware's seven subsidiaries, it provides pari-mutuel thoroughbred horseracing and greyhound racing in New York, Florida, West Virginia, Arkansas and Arizona.

Woodbine Entertainment Corp. (Woodbine), owns 2.23 percent of the outstanding ownership units issued by Empire, but holds an option to purchase additional units which, if exercised, would bring Woodbine's ownership interest to 4.92 percent. Originally incorporated in 1902 as the Toronto Driving Club, Ltd., its name was changed to the Ontario Jockey Club in 1971. In 2001, its name was, once again, changed, this time to Woodbine Entertainment Group, and is presently a not-for-profit corporation based in Toronto. Its primary business is horseracing, gaming and entertainment, and its major operations are within Canada. Woodbine also maintains business relationships in 35 states within the United States through simulcasting agreements and totalisator supply contracts. Woodbine owns and operates both Woodbine Racetrack in Toronto and Mohawk Racetrack in Campleville, Ontario.

Scientific Games Holding Corp. (Scientific Games) owns 6.81 percent of the outstanding ownership units issued by Empire. It is a wholly owned subsidiary of Scientific Games Corp., a publicly traded company traded on the NASDAQ Stock Exchange, providing services, systems and products to both the lottery and pari-mutuel wagering industries. Its products include computerized wagering systems, systems and services to horse and greyhound racetracks, off-track betting facilities, casinos, and telephone and Internet account wagering operations. It also, itself, provides race simulcasting and telecommunications services and Internet and telephone account wagering. In addition, Scientific Games maintains lottery contracts in 25 states and 50 countries.

Except for Woodbine, each of the above five corporate entities has reportedly invested \$250,000 and owns 6.81 percent of Empire. Woodbine has invested \$100,000 and owns 2.73 percent of Empire. A sixth corporate investor, National Development Investors, LLC also owns 6.81 percent of Empire. National Development was formed in 2006 for the sole purpose of investing in Empire and is owned by partners in The Cordish Company, a privately-owned real-estate development company.

It is noteworthy that when it became known that all key persons would be required to complete an extensive background questionnaire and swear to its accuracy, four individuals, at the time key persons in Empire, divested themselves of portions of their ownership shares, causing them to fall just below the 2.5 percent threshold for the definition of a key person. This reduction in ownership shares came, at least for three of the individuals, on the same day, March 29, 2007. The four individuals are:

- Robin Malatino (Diamond M Stables, LLC) reduced her shares from 2.73 percent to 2.32 percent and was removed from Empire's Board of Managers.
- Stephen Green reduced his shares by two thirds, leaving him with 2.32 percent, and was removed from Empire's Board of Managers.
- Thomas Newkirk reduced his shares from 2.73 percent to 2.32 percent and was removed from Empire's Board of Managers.
- Mary Lou Whitney reduced her shares from 4 percent to 2.32 percent.

Included as an additional person of interest is Jared Abbruzzese, a former investor and founding member of Empire's Board of Managers. He is a focus of the Special Report from Thacher Associates below and is of major significance in the section on Political Contributions and Lobbying.

Special Report from Thacher Associates

The purpose of this Memorandum is to provide a brief history of Friends of New York Racing, Inc. (“FNYR”), which has been described by the court-appointed monitor to the New York Racing Association (“NYRA”) as the “de facto” predecessor entity to Empire Racing Associates, LLC (“Empire”). To that end, this Memorandum also sets forth certain information regarding the formation of Empire.ⁱ

This Memorandum should be viewed as separate from the report provided by Thacher Associates, LLC (“TA”) to the Inspector General detailing the findings of TA’s integrity-related background investigation of Empire. The information contained herein is in part based on the views of the court-appointed monitor to NYRA. However, it is also based on the views of certain players involved in the New York racing franchise, including members of NYRA, the New York Thoroughbred Horsemen’s Association, Inc. (“NYTHA”), the New York Thoroughbred Breeders, Inc. (“NYTB”), and other entities connected to horse breeding and racing in New York.ⁱⁱ

The information contained in this Memorandum was generated by TA primarily through electronic database research and field investigations conducted in connection with TA’s background investigation into NYRA’s activities for the period from September 2005 to the present. In addition to the electronic database research conducted by TA, sources of information contained herein include interviews with the following individuals:

- Gary Contessa, former member of the Board of Trustees of NYTHA; currently associated with Excelsior Racing Associates.
- Steven Duncker, Chairman, NYRA; former Co-Chief Operating Officer, NYRA.
- Robert Flynn, Executive Director, NYTHA.
- Alan Foreman, Legal Counsel to NYTHA.
- Charles Hayward, Chief Executive Officer, NYRA.
- Neil Getnick, Managing Partner, Getnick & Getnick (NYRA’s court-appointed monitor in connection with a December 11, 2003 Deferred Prosecution Agreement between NYRA and the US Attorney’s Office for the Eastern District of New York).
- Joseph Pepe, President, Hawthorne Investigations (Getnick & Getnick’s lead investigator during the NYRA monitorship).
- Barry Ostrager, member of NYRA’s Board of Trustees; former President of NYTB; current head of Litigation at Simpson Thacher & Bartlett.
- William Woods, President, Datavision.

The detailed findings of our investigation are set forth below, in the form of a time line.

JULY 2004

In July 2004, Tim Smith (“Smith”) announced his resignation as Commissioner of the National Thoroughbred Racing Association, located in Louisville, Kentucky. NYRA’s Chairman and CEO, Barry Schwartz, had recently relinquished his CEO post, and it was rumored that Smith was to be his successor.ⁱⁱⁱ

AUGUST 2004

During the six-week season at Saratoga Racetrack in Saratoga, New York, Smith introduced himself as NYRA’s next CEO, and promoted a plan to transform the NYRA franchise into a for-profit, privately owned business.^{iv} The first phase of Smith’s plan to privatize NYRA involved the formation of a non-profit think tank called Friends of New York Racing (“FNYR”). FNYR’s stated purpose was

to study the problems of the horseracing industry in New York racing, and to propose solutions that were in the best interests of New York racing.^v

While in Saratoga, Smith met with Charles Hayward (“Hayward”). Hayward had recently retired as publisher of the Daily Racing Form, a leading publication in the thoroughbred horse racing industry. Smith informed Hayward that he was slated to become NYRA’s next CEO. He also disclosed plans to form a group whose purpose was to take the NYRA franchise private. Smith urged Hayward to consider heading FNYR, the group being formed to privatize NYRA. Hayward told Smith that he was not interested in the job.^{vi}

On August 28, 2004, Smith met with Neil Getnick (“Getnick”) and Joseph Pepe (“Pepe”). Getnick and Pepe were in the process of vetting Smith for NYRA’s CEO position. During the course of the meeting, Smith informed Getnick and Pepe that a couple of weeks earlier he had attended an organizational meeting of a group named Friends of New York Racing. Smith disclosed to Getnick and Pepe the existence of a plan to privatize NYRA; participants in the plan included a broad coalition of businesses, including Churchill Downs, Inc. (“Churchill Downs”), Scientific Games Holding Corporation, Inc. (“Scientific Games”), and Woodbine Entertainment Group (“Woodbine”). According to Smith, the discussion at the FNYR organizational meeting which he had attended had focused on a two-phased approach to the privatization drive: (1) form a non-profit advocacy group (FNYR); and (2) form a second group to operate the racing franchise once it had been privatized.^{vii}

Smith also told Getnick and Pepe that he had recently played golf with New York State Senate Majority Leader Joseph Bruno (“Senator Bruno”). According to Smith, he and Senator Bruno thought it would be a good idea to continue the Getnick & Getnick monitorship beyond its planned termination date in mid-2005.^{viii}

After the meeting, Getnick advised one of NYRA’s then Co-Chief Operating Officers, Steven Duncker (“Duncker”), about the conversation with Smith. Shortly thereafter, NYRA decided not to hire Smith as its next CEO, fearing that Smith’s plan to take NYRA private presented a potential conflict of interest.^{ix}

A few days later, Smith again met with Hayward. Smith disclosed to Hayward that he would not be NYRA’s next CEO. When Hayward asked why, Smith explained that he had “underestimated the federal monitor.” Smith told Hayward that he would now be heading up the effort to privatize NYRA, and Smith urged Hayward to pursue the CEO position at NYRA.^x

DECEMBER 2004

In December 2004, The Jockey Club formed New York Racing and Entertainment, LLC, a for-profit company, to run the New York racing franchise in the event it was taken private.^{xi} Also, Smith announced the planned formation of a non-profit planning and advocacy organization. Smith said the organization, to be known as “Friends of New York Racing, Inc.,” would be officially launched in early 2005.^{xii}

FEBRUARY 2005

At a press conference on February 18, 2005, Smith announced FNYR’s goals and the membership of the newly formed FNYR Board of Directors. The members included top executives of the following major contributors to FNYR:

- The President of Magna Entertainment Corp. (“Magna”), based in Ontario, Canada.
- The President of Churchill Downs, based in Louisville, KY.
- The President of The Jockey Club, based in Lexington, KY and New York, NY.

- The Chairman of Woodbine, based in Toronto, Canada.
- The Chairman of Scientific Games, based in New York, NY.
- The Chairman of Youbet.com, Inc. (“Youbet”), based in Woodland Hills, California.

Jared Abbruzzese (“Abbruzzese”) and NYTHA’s President, Richard Bomze, were also members.^{xiii} Magna, Churchill Downs, Woodbine, and Scientific Games, along with Abbruzzese and NYTHA, would later be prominent investors in Empire.

With respect to Youbet, it is also important to note that, in 2005, the US Attorney for the Southern District of New York announced an 88-count indictment charging 17 defendants with operating an illegal gambling business (the “Uvari Indictment”).^{xiv} The charges included conspiracy, money laundering, violations of the Wire Act, extortion, wire fraud, and horse doping; and the defendants included Gerald, Cesare and Anthony Uvari, all alleged to be associates of the Gambino organized crime family. Four off-shore rebate shops were named in the Uvari Indictment; one of these shops was International Racing Group, Inc. (“IRG”), based in Curaçao, Netherlands Antilles.

Following the Uvari Indictment, on January 27, 2005, the New York State Racing and Wagering Board (“RWB”) banned all New York horse tracks from selling their simulcast signals to ten off-track wagering firms, including IRG.^{xv} Following the RWB ban, Youbet purchased IRG.^{xvi} Youbet also purchased United Tote, one of three major totalisator companies providing pari-mutuel wagering computational and wagering transmission services to the industry.^{xvii} United Tote provided tote services to the leading offshore gaming service banned by the RWB, Racing & Gaming Services, Inc., based on the Caribbean island of St. Kitts.^{xviii}

MARCH 2005

In March 2005, FNYR formed the FNYR Political Action Committee (the “PAC”).^{xix} According to a December 2005 FNYR report, the PAC participated in “numerous events and contributions to help raise awareness of industry importance and needs (March-November).”^{xx}

JUNE 2005

In June 2005, FNYR issued a “Preliminary Report” containing its initial findings and recommendations. The report advocated that NYRA’s current assets and related wagering rights be owned and managed by a for-profit enterprise. If NYRA assets were privatized, the report estimated that (1) New York State would receive an “up-front franchise fee” of \$330 million; and (2) between \$500 million and \$900 million in capital would be needed to fund the project.^{xxi}

AUGUST 2005

In August 2005, Smith disclosed to Barry Ostrager, former President of NYTB (“Ostrager”), that he was organizing a group of people with horseracing and other important connections to take NYRA private.^{xxii} Smith claimed that if NYTB (representing the major breeders in New York State) and NYTHA (representing horse owners and trainers throughout in New York State) endorsed the group that Smith was forming, then Smith’s group would have an inside track on being awarded the racing franchise. According to Ostrager, he declined to give NYTB’s endorsement because he felt that a group funded largely by out-of-state investors would not have the best interests of New York racing at heart.^{xxiii}

Ostrager later formed the opinion that Smith’s investors were a coalition of “carpet baggers and opportunists.”^{xxiv} In Ostrager’s view, Smith’s non-profit group was purporting to make non-partisan, bidder-neutral recommendations on NYRA’s future as a public service. However, Ostrager believed that Smith’s non-profit group had a hidden agenda: FNYR was not interested in advancing the public

interest, but rather was promoting its backers' financial self-interest. Ostrager believed that all actions taken by FNYR were designed to further this undisclosed objective.^{xxv}

According to Ostrager, Smith also approached NYTHA's President, Richard Bomze ("Bomze"), seeking NYTHA's endorsement of the new venture.^{xxvi} (As events would later show, Smith had better luck with Bomze than with Ostrager.)

During the 2005 Saratoga meet, Smith also spent time with two early participants in FNYR, Abbruzzese and Robin Malatino ("Malatino").^{xxvii} At this time, Smith was talking about putting the Empire group together as a for-profit organization.^{xxviii} Smith introduced the pair to Ostrager.^{xxix} Abbruzzese was one of Smith's major backers, and Smith knew Abbruzzese had influence with Senator Bruno.^{xxx}

Abbruzzese and Malatino told Ostrager they were putting together a private investment group to take NYRA private. The pair tried to convince Ostrager to lend NYTB's name to the venture, advising Ostrager that they were experienced in initial public offerings, and that pre-public offering investors would get a rich return on their investment if the group was awarded the franchise. The also informed Ostrager that one of the reasons they wanted to control NYRA was so that they could control the lucrative VLT gambling operations.^{xxxi}

FNYR also formed a business advisory council comprised of corporate representatives and individuals, three of whom (Jeff Perlee, John Leonard, and Malatino) would later become Empire investors.^{xxxii}

Finally, also in August 2005, New York Governor George Pataki signed a law establishing a NYRA Oversight Board. The law also accelerated the process of bidding on the New York racing franchise, and authorized the installation of additional VLTs.^{xxxiii}

SEPTEMBER 2005

Getnick & Getnick, NYRA's court-appointed monitor, issued a final report on its monitorship of NYRA and, upon the motion of the US Attorney's Office, the court dismissed the NYRA indictment.

NOVEMBER 2005

In late November 2005, Senator Bruno held a meeting in his Albany office to discuss NYRA's status. Hayward and other NYRA officials attended, including NYRA Trustee Wayne Barr, who happened to be Abbruzzese's business partner. Also present were Senator Bruno and three top aides, Ken Riddett, Mike Avela and Heather Mowatt, and a veterinarian named Jerry Belinski. Joseph Toranni ("Toranni"), Senator Bruno's appointee to a NYRA Oversight Committee, participated by phone.^{xxxiv}

NYRA's co-Chief Operating Officer, Duncker, was absent because a request had been made that he not participate.^{xxxv} According to Hayward, Senator Bruno did most of the talking. The Senator was very critical of NYRA, and he denigrated Duncker and Peter Karches. During the meeting, Toranni asked Hayward to call him after the meeting was over.^{xxxvi}

Hayward called Toranni after the meeting, and Toranni told him that Senator Bruno wanted (1) Duncker and Karches to resign; (2) Smith to be involved in the franchise selection process; and (3) to accelerate the transfer of NYRA's franchise.^{xxxvii}

DECEMBER 2005

In December 2005, FNYR issued its last report, “The Way Forward.” One recommendation made by FNYR in the report was that New York State make cash advances to an “Oversight Board” to fund racing franchise operations in the event NYRA declared bankruptcy. Another recommendation was to accelerate the process of awarding the racing franchise.^{xxxviii}

EARLY 2006

In early 2006, Empire was formed, and FNYR was later dissolved.

MARCH 2006*Confidential Offering Memorandum*

Through a Confidential Offering Memorandum, dated April 2006 (the “Offering Memorandum”), Empire solicited qualified investors to purchase membership units, priced at \$10 per unit, in order to raise \$3 million. The Offering Memorandum’s introductory paragraph states: “[Empire] is a newly formed limited liability company organized by owners and breeders of New York racehorses to operate New York race tracks and related gaming businesses”^{xxxix}

Operating Agreement

Empire’s Operating Agreement, dated March 22, 2006 (the “Operating Agreement”), identifies Empire’s initial members as follows:^{xl}

1. Bazaguma, LLC d/b/a Weather Watch Farm (attention Jared E. Abbruzzese, Sr.).
2. Diamond M Sable, LLC (attention Robin Malatino).
3. Thomas R. Newkirk.
4. Jeffrey Tucker.

Amendment to Operating Agreement

An Amendment to the Operating Agreement, purporting to be effective as of March 27, 2007 (the “Operating Agreement Amendment”), added a new Section 13.10 to the Operating Agreement.^{xli} This new Section 13.10, entitled “Company Call of Member Interests”, provides Empire with greater flexibility with respect to authorizing the repurchase and transfer of membership interests.

CONTRIBUTORS TO FNYR

According to FNYR, each of ten “Founding Contributors” contributed \$100,000 or more to FNYR, including the following: Churchill Downs; Magna; Scientific Games; Woodbine; Youbet; Capital & Technology Advisors (the firm run by Jared Abbruzzese); and The Jockey Club.^{xlii} The specific amounts contributed by each entity are not listed.

FNYR described another category of members as “Charter Members”, each of whom contributed \$50,000 or more. NYTHA was one of three Charter Members listed.^{xliii} However, NYTHA had only contributed \$20,000.^{xliv}

FNYR described a third category of members as “Sustaining Members”, each of whom contributed \$25,000 or more. One of the Sustaining Members was Delaware North Companies. A subsidiary of Delaware North Companies, Delaware North Companies Gaming & Entertainment, Inc. (“DNCG&E”), became a major Empire investor the following year.^{xlv}

In the Smith Letter, Smith disclosed that The Jockey Club had initially committed \$1 million to FNYR. However, in point of fact, The Jockey Club contributed only \$500,000, withholding the other \$500,000 to permit The Jockey Club “to invest in the subsequent operating business, when and if it materialized.”^{xlvi}

INVESTORS IN EMPIRE

Five of FNYR’s ten Founding Contributors - Churchill Downs, Magna, Scientific Games, Woodbine, and Abbruzzese - were among Empire’s initial top investors. Each invested \$250,000 in Empire, entitling each to 25,000 units, or 6.1% of the total number of units issued by Empire.^{xlvii}

Woodbine, also a major FNYR contributor, reportedly invested \$175,000 in Empire, entitling it to 17,500 units, or 4.2% of the total number of units issued by Empire.^{xlviii} (However, documentation reviewed by TA indicates that Woodbine did not actually invest any cash. Instead, Empire issued 10,000 units, valued at \$100,000 to Woodbine as consideration for consulting services provided by the company to Empire. Please see the section below entitled “Woodbine Subscription Agreement” for additional information regarding Woodbine’s investment in Empire.)

NYTHA has also been listed as a major initial investor in Empire, having reportedly invested \$123,098 in the company, entitling it to 12,310 units, or 3% of the total number of units issued by Empire.^{xlix} (However, NYTHA did not invest any cash; it received its units as consideration for the endorsement by its Board of Trustees of Empire’s bid for the racing franchise.)¹

DNCG&E has also been listed as a major Empire investor, having invested \$250,000 in the company, representing 25,000 units, or 6.1% of the total number of units issued by Empire.ⁱⁱ

NYTHA

In March 2006, Smith addressed the NYTHA Board of Trustees in executive session.ⁱⁱⁱ No minutes were kept of the meeting. Smith handed out a proposed NYTHA resolution addressing NYTHA’s exclusive endorsement of a company called the New York Owners Coalition, LLC (“NYOC”).^{liii} Smith told the NYTHA board that NYOC was attempting to obtain the NYRA racing franchise; the proposed NYTHA resolution distributed by Smith endorsed NYOC, in exchange for a 1% ownership interest by NYTHA in NYOC.^{liv} The proposed resolution made no reference to allocating any seats on NYOC’s board to NYTHA members.

Contessa recalled that during Smith’s 20-minute presentation to the board he made a pitch for the Executive Committee’s endorsement. Smith said that his group would embrace the horsemen and allow the horsemen to invest. Contessa recalled Smith mentioning that if a horseman invested \$50,000, he/she would probably get back \$1 million.^{lv} After Smith’s presentation, NYTHA’s Executive Committee voted 9 to 1 to support Smith’s request for NYTHA’s endorsement, subject to further negotiations regarding NYTHA’s participation in Empire.^{lvi} Executive Committee member Mike Shanley was the sole “no” vote.^{lvii}

After subsequent negotiations, NYTHA’s interest in Empire was increased to 3%, and NYTHA was given two seats on Empire’s Board of Managers. Justin McDonald (“McDonald”), a former FNYR staff member and current Empire officer, prepared a new resolution for NYTHA entitled “Proposed Resolutions Relating to ERA.” The language in the new resolution included the following language:^{lviii}

- “[Empire] was formed by New York horsemen (NYTHA members) who have extensive business and investment experience in order to provide an entity for all New York horsemen to participate in during the upcoming bid process to be conducted by New York State for the Franchise.”

- “[Empire] will be seeking to offer and sell approximately \$3 million of equity to NYTHA members who are also ‘accredited investors’ under the relevant securities laws, in an effort to raise the capital necessary to further develop and implement [Empire]’s plan.”
- “[Empire] is offering membership interest units equal to 3% of [Empire] to NYTHA in exchange for its exclusive endorsement and support of [Empire] and its efforts to secure and manage the Franchise; provided, that such 3% interest shall be non-dilutable relative to the initial financing phase (e.g., \$3 million); and provided, further, that such equity interest shall not entail any financial liability to NYTHA or its members.”
- “NYTHA has been allocated two seats on the Board of Managers of [Empire] and has appointed Charles Reiss and Terry Finley as its representatives.”^{lix}

TA was advised by NYTHA’s counsel that the NYTHA board passed this resolution by the same 9 to 1 vote.^{lx}

The day after Smith’s presentation, NYTHA’s Executive Committee held a conference call to further discuss the Empire proposal. Contessa recalled that the conversation became heated when it was disclosed that Reiss had already made a personal investment in Empire.^{lxi,11} Contessa informed TA that the day after the conference call, he resigned from NYTHA’s board.^{lxii} (Contessa was not certain whether it came out during this conference call or at a later date that Terry Finley had also already made a personal investment in Empire.¹² In addition, according to Contessa, an alternate member of NYTHA’s board, Martin Cunningham, had also already made a personal investment in Empire.)^{lxiii}

Contessa said that a couple of days after the NYTHA vote, Dennis Brida (“Brida”), a former NYTHA President and a member of the FNYR board, met with Contessa and tried to persuade him to invest \$50,000 in Empire.^{lxiv} (Brida was the Executive Director of the NYTB from April 2002 to April 2006, and he has served as Empire’s Executive Vice President since May 2006. Brida’s wife, Juliane, is an Empire investor.)¹³

Brida served as President of NYTHA from 1997 to 2000, and it has been reported that he hand-picked his successor, current NYTHA President Richard Bomze.^{lxv} According to Contessa, Bomze fought for NYTHA to endorse Empire.^{lxvi}

In early March 2006, Empire’s CEO, Jeff Perlee (“Perlee”), advised the Daily Racing Form that Smith “was not involved in the formation of Empire.”^{lxvii} However, a few weeks later, Smith acknowledged his involvement in forming Empire.^{lxviii}

APRIL 2006

On April 6, 2006, Perlee wrote a letter to NYTHA in which he referenced the Operating Agreement, and advised NYTHA that, as contemplated by the Operating Agreement, NYTHA had been admitted as a member of Empire. According to the letter, NYTHA would hold 3% of the Empire units issued during “phase I”, and NYTHA members Reiss and Finley would serve on Empire’s Board of Managers. The terms of Perlee’s letter were accepted and agreed to by Bomze on NYTHA’s behalf.^{lxix}

May 2006

¹¹ According to a letter dated July 12, 2007 from Empire Racing CEO Jeff Perlee (the “July 12, 2007 Perlee letter”), Charles Reiss did not invest in Empire Racing until July 30, 2006.

¹² According to the July 12, 2007 Perlee letter, Terry Finley did not invest in Empire until September 27, 2006.

¹³ According to the July 12, 2007 Perlee letter, Dennis Brida specifically denies the facts as relayed by Contessa.

In May 2006, Smith became an investor in Empire. He publicly acknowledged his financial interest in August 2006.^{lxx}

JUNE 2006 THROUGH OCTOBER 2006

Empire Subscription Agreements

Empire provided TA with a binder entitled “Subscription Documents and Investor Information” (the “Binder”). The Binder included the following documents:

- The Empire Subscription Agreement (the “Master Subscription Agreement”).^{lxxi}
- Signature pages to the Master Subscription Agreement from 33 Empire members; signature pages were not provided for Andrew Mathias, Tom Newkirk, Debra Roma, Jeffrey Tucker, Backstretch Employee Service Team, Diamond M Stable LLC, NYTHA, and the Empire Employee Plan).^{lxxii}
- A separate subscription agreement between Empire and NYRHC, LLC (the “NYRHC Subscription Agreement”).^{lxxiii}
- A separate subscription agreement between Empire and Woodbine (the “Woodbine Subscription Agreement”).^{lxxiv}
- A letter from Empire to NYTHA, dated April 6, 2006, acknowledging NYTHA’s status as a member of Empire, and its ownership of units equal to 3% of the total number of units issued by Empire in “phase 1.”

Master Subscription Agreement

As noted above, Empire informed TA that all initial Empire investors, other than Woodbine and NYRHC, executed the Master Subscription Agreement.

With respect to Magna’s investment in Empire, TA specifically requested Empire to produce any and all related documents, including, but not limited to, private placement memoranda, memoranda of understanding, consulting agreements, warrants and repurchase agreements in which Empire is a party with Magna. Empire responded to TA’s request by informing TA there were no such documents. However, as noted below (see “NYRHC Subscription Agreement”), Magna is signatory to a Memorandum of Understanding, dated August 15, 2006 (the “August 15 MOU”), among Empire, Magna, Churchill Downs, and DNCG&E.

With respect to DNCG&E’s investment in Empire, TA requested Empire to produce any and all related documents, including, but not limited to, private placement memoranda, memoranda of understanding, consulting agreements, warrants and repurchase agreements in which Empire is a party with DNCG&E. Empire responded to TA’s request by providing TA with a copy of a Memorandum of Understanding, dated July 7, 2006 (the “July 7 MOU”), between Empire and DNCG&E.^{lxxv} Empire also provided TA with the first and last page of the August 15 MOU.

With respect to Scientific Games’ investment in Empire, TA requested Empire to produce any and all related documents, including, but not limited to, private placement memoranda, memoranda of understanding, consulting agreements, warrants and repurchase agreements in which Empire is a party with Scientific Games. Empire responded to TA’s request by providing TA with a copy of a Memorandum of Understanding, dated August 10, 2006 (the “August 10 MOU”), between Empire and Scientific Games.^{lxxvi}

Woodbine Subscription Agreement

The Woodbine Subscription Agreement appears to reflect circumstances unique to Woodbine’s investment in Empire. Paragraph 1 of the Woodbine Subscription Agreement, entitled “Compensation

under the Consulting Agreement”, references a Consulting Agreement between Empire and Woodbine, dated July 14, 2006 (the “Woodbine Consulting Agreement”), the terms of which entitle Woodbine to compensation for services “upon the occurrence of certain events.”^{lxxvii} Paragraph 1 notes that these unspecified events have occurred, and that Woodbine is entitled to receive (1) 10,000 units valued at \$100,000; and (2) a warrant to acquire an additional 7,500 units, valued at \$75,000, as compensation for the provision of services (the “Woodbine Warrant”).^{lxxviii}

The value of Woodbine’s compensation under the Woodbine Consulting Agreement, combined with the face value of the unexercised Woodbine Warrant, total \$175,000, or the amount reported by Empire in August 2006 as Woodbine’s investment in the company.^{lxxix} Although the general nature of the services to be provided by Woodbine to Empire is described in the Woodbine Consulting Agreement, the fair market value of these services is not known. Consequently, it would appear that the document Empire submitted to the Ad Hoc Committee in early 2007, which indicated that Empire had closed its initial private offering with total capitalization of \$4,103,261, including a \$175,000 investment by Woodbine, was inaccurate.

The Woodbine Subscription Agreement makes reference to a Private Placement Memorandum, dated April 2006. Justin McDonald of Empire informed TA that this reference was incorrect, and that it should have been to the Offering Memorandum; according to McDonald, no Private Placement Memorandum has ever existed.

NYRHC Subscription Agreement

The NYRHC Subscription Agreement makes reference to a Private Placement Memorandum, dated March 2006, and to a Memorandum of Understanding, dated August 15, 2006 (the “August 15 MOU”), among Empire, Churchill Downs, Magna, and DNCG&E.^{lxxx}

The NYRHC Subscription Agreement stipulates that Empire is obligated to amend the Operating Agreement as required by Section 1 of the MOU (the “Amendment Requirement.”) Specifically, Paragraph 5 of NYRHC, LLC’s subscription agreement, entitled “Repurchase Obligation,” includes the following language:

“[P]ursuant to Section 15(f) of the MOU, if the Investor terminates the MOU in accordance with Section 15(f) of the MOU, including, without limitation, as a result of the Company’s [Empire’s] failure to satisfy the Amendment Requirement, then the Company [Empire] will be obligated to repurchase from the investor the 25,000 units . . . for an aggregate purchase price of \$250,000.”^{lxxxi}

The terms of the August 15 MOU stipulate that Churchill Downs and Magna may terminate the August 15 MOU under certain circumstances, including in the event Empire (1) fails to perform its obligations in any material respect, (2) files for or is the subject of bankruptcy proceedings, or (3) made any representation or warranty that was false in any material respect and does not cure the falsity. Upon such termination, Empire is required to purchase Churchill Downs’ and Magna’s equity membership units for \$250,000.

The terms of the Operating Agreement Amendment referred to earlier do not appear to satisfy the requirements set forth in Section 1 of the August 15 MOU. Consequently, it does not appear that, to date, Empire has complied with the Amendment Requirement.

Paragraph 4 of the August 15 MOU, entitled “OperationsCo”, requires Empire to retain the services of an entity called OperationsCo, which is described as “a joint venture owned 50% by DNCG&E, 25%

by Churchill Downs, and 25% by Magna, to provide management services with respect to the Racing Franchise...^{lxxxii}

Paragraph 7 of the August 15 MOU, entitled “DistributionCo”, indicates that a limited liability will be created by Empire, Churchill Downs, and Magna to license and distribute the racing franchise’s content rights. Empire will own 50% of this new entity, and Churchill Downs and Magna will each own 25% of the entity. Churchill Downs and/or Magna will be designated as DistributionCo’s exclusive agent for “licensing and distributing the Content Rights to all domestic and international distribution channels.” Initially, Empire will receive 100% of DistributionCo’s earnings until a threshold is reached, and afterwards Empire will be entitled to retain 50% of the earnings and Churchill Downs and Magna will be entitled to receive 25% each.

AUGUST 2006

On August 1, 2006, at an Albany Law School Conference in Saratoga Springs, Hayward challenged Smith’s roles in FNYR and Empire.^{lxxxiii} On August 4, Smith circulated a six-page letter to the participants in FNYR, responding to questions raised about FNYR’s objectivity and good faith. Smith indicated that around the first three months of 2006, as FNYR was winding down, “the concept of a New York industry-centric bidding group, including the horsemen’s association, began to take shape.” Smith claimed that he encouraged the representatives of this potential organization and offered some ideas about getting organized.^{lxxxiv}

In the letter, Smith disclosed The Jockey Club’s initial commitment of \$1 million to FNYR and The Jockey Club’s formation of a for-profit company in late 2004. Smith claimed that The Jockey Club’s for-profit business was not pursued because it could be perceived as compromising the credibility of FNYR’s non-profit activities. Simultaneously, The Jockey Club held back \$500,000 of its FNYR contribution to permit it to invest in the operating company if one materialized.^{lxxxv}

NOVEMBER 2006

Eliot Spitzer was elected Governor of New York.

DECEMBER 2006

An FBI investigation of Senator Bruno became public.

FEBRUARY 2007

The Ad Hoc Committee on The Future of Racing completed its process for selecting the next franchise owner. The committee selected Excelsior Racing Associates.

MARCH 2007

Governor Spitzer formed a special panel to revisit the selection process. Certain of Empire’s members sold a portion of their membership interests in order to avoid having to make full financial disclosure to TA (among these members was Malatino).

CONCLUSION

It is important to note that many of the individuals interviewed in connection with TA’s investigation into the history of FNYR and the formation of Empire have a vested interest in assuring that Empire is not awarded the New York racing franchise. However, our findings indicate that, if no other definitive conclusions can be reached regarding the true genesis of Empire, it appears clear that Tim Smith was,

contrary to his and Empire's published denials, a critical part of the company's formation. Why Smith and Empire chose to mask Smith's involvement in the venture remains unclear.

In an odd twist, Ostrager informed TA that in late 2006 Smith told an acquaintance that he would not "take the fall" for "what had happened," and that if he went down, others would go down with him.^{lxxxvi} While the statement raises concerns, TA is unable to ascertain the context in which Smith made the statement. Consequently, we are unable to ascribe any meaning whatsoever to the fact that the statement may have been made, as was reported by Ostrager.

Finally, at a public hearing in Albany, NY in April 2007, Empire told of its being formed by New York horsemen for New York horsemen. In response to a panel question expressing concern about what would happen if Empire won the bid, and whether Churchill Downs and Magna would take control of Empire, Empire's Chairman, Jeffrey Tucker, assured the panel that the New York horsemen would always be in control.^{lxxxvii}

Empire, like any other franchise bidder, will need to raise significant amounts of capital to operate the franchise. The raising of such funds will almost certainly result in significant changes to Empire's capital structure. As a result, Empire's history may not be any indication of its future.

ⁱ In a press release issued by Empire on April 10, 2007, entitled "Empire Racing sets the Bar for New York's Racing Industry – Most Experienced and Tested Management Team in the History of Thoroughbred Racing Defines Racing's Potential for New York's Economy", Empire stated that "New York's horsemen community formed Empire Racing as a solution to the many problems created by the failures of the racing franchise's current operator" and that "Empire Racing is a group of visionary New York horsemen and breeders seeking to revive NY racing by securing the exclusive right to operate the three New York thoroughbred racetracks." This press release has been attached hereto as Exhibit 1.

ⁱⁱ It should be noted that a number of these individuals are currently connected to entities in competition with Empire with respect to the award of the New York racing franchise.

ⁱⁱⁱ Interview of Charles Hayward on April 13, 2007 ("Hayward Interview 1"); meeting with Neil Getnick and Joseph Pepe on April 19, 2007 ("Getnick & Pepe Meeting").

^{iv} Ibid.

^v Ibid.

^{vi} Hayward Interview 1.

^{vii} Getnick & Pepe Meeting.

^{viii} Getnick & Pepe Meeting.

^{ix} Telephone interviews of Neil Getnick and Steven Duncker in late April 2007.

^x Hayward Interview 1.

^{xi} See letter from Tim Smith to "Friends of New York Racing Board of Directors; Business Advisory Council Members; and Key Contributors, Staff Members, Consultants, Advisors", dated August 4, 2006 (the "Smith Letter"), attached hereto as Exhibit 2.

^{xii} See press release issued by the National Thoroughbred Racing Association ("NTRA"), dated December 16, 2004, attached hereto as Exhibit 3. See also article from the Daily Racing Form, dated August 9, 2006, entitled: "Former NTRA Commissioner Comes Full Circle," attached hereto as Exhibit 4.

^{xiii} See Preliminary Report of Friends of New York Racing, dated June 27, 2005 ("FNYR Preliminary Report"), Appendix C pages 132-134, attached hereto as Exhibit 5. See also press release issued by FNYR, dated February 18, 2005, entitled: "Friends of New York Racing get Organized," attached hereto as Exhibit 6.

^{xiv} *United States v Gerald Uvari, et al.*, 05 CR 24, SDNY. A copy of the January 10, 2005 indictment has been attached hereto as Exhibit 7.

^{xv} See letter from the RWB to "All New York State Racetrack Presidents and General Managers", dated January 27, 2005 ("RWB Letter"), attached hereto as Exhibit 8.

^{xvi} See press released issued by Youbet, dated February 8, 2005, entitled "Youbet.com Agrees to Acquire International Racing Group," attached hereto as Exhibit 9. See also press release issued by Youbet, dated June 2, 2005, entitled "Youbet.com Completes Acquisition of International Racing Group," attached hereto as Exhibit 10.

^{xvii} Tote systems form the neural network of the pari-mutuel system; every wager into a thoroughbred racetrack's pari-mutuel pool, no matter where the bet originates in the world, is anonymously processed through a tote system. Within the industry, it is known that the system can be manipulated to fraudulently "past post" bets after a race has started.

^{xviii} See RWB letter; Getnick & Pepe Meeting; telephone interviews on April 20, 2007 and May 8, 2007 with William Woods.

^{xix} See report issued by FNYR in December 2005, entitled "The Way Forward, Report and Recommendations, Friends of New York Racing, Inc." ("FNYR Report and Recommendations"), Appendix B page 17, attached hereto as Exhibit 11.

^{xx} Ibid.

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- ^{xxi} See FNYR Preliminary Report, Appendix A pages 77-79, attached hereto as Exhibit 12.
- ^{xxii} Telephone interviews of Barry Ostrager on April 17, 2007 and April 18, 2007 (“Ostrager Interviews”).
- ^{xxiii} Ibid.
- ^{xxiv} Ibid.
- ^{xxv} Ibid.
- ^{xxvi} Ibid.
- ^{xxvii} Ibid. Both Abbruzzese and Malatino later became two of Empire’s initial four investors.
- ^{xxviii} Telephone interviews of Alan Foreman on April 16, 2007 and April 19, 2007 (“Foreman Interviews”).
- ^{xxix} Ostrager Interviews.
- ^{xxx} Ibid. See article from The Times Union, dated December 31, 2006, entitled “Bruno Friend Draws Scrutiny from FBI; Senate Majority Leader, Business Associate Have Tangled Relationship,” attached hereto as Exhibit 13. See also article from The New York Times, dated January 11, 2007, entitled “Bruno Son Emerges as Key Link in Father’s Circle of Connections,” attached hereto as Exhibit 14.
- ^{xxxi} Ibid. According to Ostrager, he knew of no one who was interested in owning the NYRA franchise prior to the advent of VLTs.
- ^{xxxii} The members of the FNYR Business Advisory Council are identified on the inside cover of the FNYR Report and Recommendations; see Exhibit 15 attached hereto.
- ^{xxxiii} Senate Bill No. 5923 created an Oversight Board for NYRA, tasked with monitoring and reviewing all aspects of NYRA’s business practices during the remainder of its franchise. The new law accelerated, to December 1, 2005 (from an original date of July 2006), the establishment of an Ad Hoc Committee to solicit proposals for the purchase of NYRA’s franchise.
- ^{xxxiv} Telephone interview of Hayward on April 24, 2007 (“Hayward Interview 2”).
- ^{xxxv} Ibid.
- ^{xxxvi} Ibid.
- ^{xxxvii} Ibid. See article in news.bloodhorse.com, dated December 13, 2005, entitled “Report: New York Must Overhaul Racing Laws,” attached hereto as Exhibit 16.
- ^{xxxviii} See FNYR Report and Recommendations, page 6, attached hereto as Exhibit 17.
- ^{xxxix} A copy of the Offering Memorandum, as provided by Empire to TA, has been attached hereto as Exhibit 18.
- ^{xl} An unexecuted copy of the Operating Agreement, as provided by Empire to TA, has been attached hereto as Exhibit 19. See Schedule A of the Operating Agreement for a list of initial members and contributions; Schedule B for a list of members of the Board of Managers; and Schedule C for a list of officers.
- ^{xli} An unexecuted copy of the Operating Agreement Amendment, as provided by Empire to TA, has been attached hereto as Exhibit 20.
- ^{xlii} See FNYR Report and Recommendations, page 19, attached hereto as Exhibit 21.
- ^{xliii} Ibid.
- ^{xliv} Interview of Robert Flynn (“Flynn”) on April 11, 2007 and follow-up telephone interview of Flynn on April 19, 2007 (collectively, the “Flynn Interviews”). Flynn provided TA with a copy of a document reflecting a contribution made by NYTHA to FNYR on September 16, 2005 in an amount equal to \$20,000. A copy of this document has been attached hereto as Exhibit 22.
- ^{xlv} See footnote (42).
- ^{xlvi} See footnote (11).
- ^{xlvii} See Exhibit 23 for a list of entities/individuals who were investors in FNYR and Empire, together with investment amounts. See also Empire’s response to the “Ad Hoc Committee on the Future of Racing’s ‘Request for Proposal’ for the New York State Racing Franchise,” dated August 29, 2006 (the “August 2006 Proposal”), Part III, Section 5.8, page 154, attached hereto as Exhibit 24.
- ^{xlviii} Ibid.
- ^{xlix} Ibid.
- ¹ Telephone interviews of Alan Foreman on April 16, 2007 and April 19, 2007 (collectively, the “Foreman Interviews”). During the Flynn Interviews, Flynn described NYTHA’s interest in Empire as a “non-equity” interest.
- ^{li} See footnote (47).
- ^{lii} Telephone interview of Gary Contessa on April 18, 2007 (“Contessa Interview”).
- ^{liii} Foreman Interviews. A copy of the proposed NYTHA resolution endorsing the NYOC is attached hereto as Exhibit 25.
- ^{liv} Foreman Interviews.
- ^{lv} Contessa Interview.
- ^{lvi} Foreman Interviews.
- ^{lvii} Contessa Interview.
- ^{lviii} Foreman Interviews. A copy of the proposed NYTHA resolution endorsing Empire has been attached hereto as Exhibit 26.
- ^{lix} It is important to note that members of NYTHA later learned that Charles Reiss and Terry Finley had each already invested individually in Empire (Contessa Interview).
- ^{lx} Foreman Interviews.
- ^{lxi} Contessa Interview.
- ^{lxii} Ibid.

^{lxiii} Ibid.

^{lxiv} Ibid.

^{lxv} Ibid.

^{lxvi} Ibid.

^{lxvii} See article in the Daily Racing Form, dated March 7, 2006, entitled "N.Y. Horsemen Support New Franchise Bidders," attached as Exhibit 27 hereto.

^{lxviii} See article in the Daily Racing Form, dated August 2, 2006, entitled "Smith says he made Investment in Empire," attached as Exhibit 28 hereto.

^{lxix} See letter from Empire to NYTHA, dated April 6, 2006, attached hereto as Exhibit 29.

^{lxx} See footnote (68).

^{lxxi} A copy of the Master Subscription Agreement, as provided by Empire to TA, has been attached hereto as Exhibit 30 (the signature pages provided by Empire to TA have not been included in the exhibit). Justin McDonald of Empire informed TA that all of Empire's initial investors, except for NYRHC, LLC and Woodbine, are signatories to the Master Subscription Agreement. According to McDonald, NYRHC, LLC and Woodbine executed separate subscription agreements with Empire; these two separate subscription agreements have been attached to this Memorandum as exhibits (as described below).

^{lxxii} Andrew Mathias, Debra Roma and the Backstretch Employee Service Team all became members of Empire on March 29, 2007 as a result of unit transfers by existing Empire members; Empire provided TA with Assignment and Assumption Agreements for each of these three transfers.

^{lxxiii} A copy of the subscription agreement between Empire and NYRHC, LLC has been attached hereto as Exhibit 31. It should be noted that NYRHC, LLC was formed by Churchill Downs for the sole purpose of investing in Empire.

^{lxxiv} A copy of the subscription agreement between Empire and Woodbine has been attached hereto as Exhibit 32.

^{lxxv} An executed copy of the July 7 MOU has been attached hereto as Exhibit 33. Among the provisions included in the July 7 MOU are, if Empire is awarded the New York racing franchise: (1) Empire's agreement to retain DNCG&E to provide management services with respect to pari-mutuel wagering and hospitality management services; (2) Empire's agreement to retain DNCG&E as an interim video machine gaming advisor; (3) Empire's agreement to pursue good faith negotiations with DNCG&E regarding the terms and conditions under which DNCG&E would provide gaming management and related services; and (4) DNCG&E's right of first refusal with respect to the provision of gaming management and related services.

^{lxxvi} An executed copy of the August 10 MOU has been attached hereto as Exhibit 34. Among the provisions included in the July 7 MOU are, if Empire is awarded the New York racing franchise: (1) Empire's and Scientific Games' agreement to pursue good faith negotiations with respect to the terms and conditions under which Scientific Games would provide the tote system and related services; and (2) Scientific Games' right of first offer with respect to management of the tote system.

^{lxxvii} An executed copy of the Woodbine Consulting Agreement has been attached hereto as Exhibit 35.

^{lxxviii} An unexecuted copy of the Woodbine Warrant, as provided by Empire to TA, has been attached hereto as Exhibit 36.

^{lxxix} See footnote (47).

^{lxxx} An executed copy of the August 15 MOU has been attached hereto as Exhibit 37. McDonald informed TA that the reference to the Private Placement was incorrect, and that it should have been to the Offering Memorandum; according to McDonald, no Private Placement Memorandum has ever existed.

^{lxxxii} See footnote (73).

^{lxxxiii} See footnote (80).

^{lxxxiiii} Hayward Interview 1.

^{lxxxv} See footnote (11).

^{lxxxvi} Ibid.

^{lxxxvii} Telephone interview of Ostrager on April 25, 2007.

^{lxxxviii} Hearing before the Governor's Special Panel, April 10, 2007. Ostrager described Tucker's statement as "preposterous" (Ostrager Interviews).

Affiliations with Rebate Shops

An issue of particular significance relating to Empire is that of the business relationships between its five corporate members and a number of the so-called rebate shops and simulcasting services that are banned from doing business in New York by the New York State Racing and Wagering Board, the so-called “NYRA Ten.” While, as set out in detail earlier in this Report, offshore rebate shops and simulcasting services are in a unique position to launder illicit monies, facilitate tax-related crimes and have, in some instances, been associated with race fixing and the doping of horses, rebate shops have not, per se, been banned from doing business with New York State racetracks. Nor have rebate shops and simulcasting services been banned in other states. They have, in fact, become a major component of the horseracing industry.

While Empire, as an entity, has committed to not having any dealings with any of the offshore rebate shops banned by the New York State Racing and Wagering Board, all five of its racing-related corporate members, representing approximately 30 percent of its ownership, have business relationships with these companies. All five are involved with such entities, either through the racetracks they own in states other than New York, or by supplying equipment, such as totalisators. In addition, a number of Empire’s corporate members have business relationships with Hipodromo de Agua Caliente, S.A. de C.V. (“Grupo Caliente”), a bookmaker and simulcaster based in Tijuana, Mexico and linked to money-laundering activities for a major Mexican drug cartel (see above for details).

Again, while the involvement of these Empire members with offshore rebate shops is not, in and of itself, illegal or a per se indication of an integrity-related problem,

these relationships should be given increased scrutiny and should be examined on a case by case basis. Moreover, as certain of these relationships are with rebate shops and simulcasters currently banned in New York State, Empire's commitment that it will not, itself, have any dealings with these banned entities should be formalized if Empire were to receive the franchise award. The specific relationships between Empire's corporate members and these banned entities are discussed below.

Magna has commercial relationships with various offshore rebate shops and simulcasting services including International Racing Group and the Elite Turf Club, both of which are among the banned NYRA Ten. Magna also does business with Grupo Caliente, its history being discussed above.

International Racing Group (IRG) is one of the rebate shops named in the *Uvari* Indictment (see above) and, consequently, included in Racing and Wagering's banned list. It is based in Curaçao, Netherlands Antilles and is a subsidiary of Youbet.Com, Inc. (Youbet), a supplier of technology and pari-mutuel horseracing data via Internet and telephone platforms. Youbet supplies totalisator systems, terminals, and other pari-mutuel wagering services and systems to the pari-mutuel industry through its subsidiary, United Tote. According to Youbet's website, its subsidiary, International Racing Group, is the only offshore "pari-mutuel wagering company" (rebate shop) to be licensed by a U.S. racing regulatory jurisdiction.

Youbet has been investigated by the Los Angeles District Attorney's Office for violating California's Internet gambling statutes. According to a January 14, 2000 report in the *E-Commerce Times*, Youbet agreed to pay \$1.3 million to California authorities to

settle an investigation into its on-line horseracing operations in the state, along with a \$600,000 civil fine. Youbet also agreed to donate \$500,000 to charitable causes and to reimburse Los Angeles County for approximately \$200,000 in investigative costs. It reportedly agreed to refrain from conducting business with California residents, although it was permitted to maintain its operations in the state. In exchange, the State of California agreed not to pursue criminal charges against Youbet or any of its corporate officers.

According to Magna, following the *Uvari* Indictment, Magna conducted a due diligence review of International Racing Group and, based upon the results of that review, Magna continues to conduct business with IRG, a rebate shop still banned in New York.

Elite Turf Club (Elite), based in Curaçao, the Netherlands Antilles, was named in the *Uvari* Indictment and, as a result, banned in New York as part of the NYRA Ten. Magna states that following the indictment, it conducted a due diligence review of Elite and, based upon the results of that review, Magna continues its business relationship with Elite.

Magna also has a business relationship with Futuristic Entertainment Holdings, Inc. (Futuristic), which is reported to be an offshore gambling operation registered in Barbados and linked to Andrew Stronach, son of Magna Chairman Frank Stronach. Andrew Stronach served as Vice President of Magna until at least 2002, and it was reported in the Canadian media that Futuristic was, at one time, owned by Magna.

Other rebate shops and simulcasting services having business relationships with Magna include Newcote Sources, Ltd. in Gibraltar; America TAB, Ltd., located at Oregon International Airport, providing Internet and telephone account wagering services; and Racing Channel/Racing Network, with Racing Channel operating within the United States; and Racing Network operating a call center in the West Indies and servicing the European market through offshore rebate shops.

Magna itself has entered the off-site account wagering business through its various affiliated companies. While a number of states, including Texas, Illinois, Michigan and Minnesota, have informed Magna that Internet wagering from residents of those states is illegal under state law, Magna, as have other similar companies, has taken the public position that there is no legal violation and continues its operations. The issue has remained largely unresolved.

Churchill Downs has commercial arrangements with various offshore rebate shops and simulcasting services, including three that are included in the NYRA Ten, along with Grupo Caliente; International Racing Group (IRG); Elite Turf Club; and Tonkawa Indian Reservation. Each is an offshore rebate shop named in the *Uvari* Indictment and banned from doing business in New York State. Following the *Uvari* Indictment, Churchill Downs suspended sending its simulcast signal to the three, but has since restored its transmission.

Churchill Downs also does business with another rebate shop named in the *Uvari* Indictment and originally part of the NYRA Ten: Lakes Region Greyhound Park (Lodge at Belmont). It was removed by the New York Racing and Wagering Board from the

banned list in late 2006, and, thus, is no longer barred from conducting business with New York State tracks.

Racing and Gaming Services, Inc. (RGS), located on the Caribbean Island of St. Kitts is one of the most successful offshore rebate shops in the industry. Because RGS's customers consistently won, at the end of each monthly settlement cycle, tracks with which RGS did business owed RGS large sums of money. Rather than accept payment directly from these tracks, RGS employed Churchill Downs as a settlement agent to collect monies from the tracks and transfer these monies to RGS. In return, Churchill Downs receives a percentage of the monies it collects. While RGS was originally named as part of the NYRA Ten and on Racing and Wagering's banned list, it was removed from the list by Racing and Wagering in late 2006.

Churchill Downs stated that as part of its long term business relationship with Grupo Caliente, it reportedly conducted a limited due diligence review and, as a result, continues to do business with the entity. Churchill Downs also conducts business with The Racing Channel, Inc./The Racing Network International (see above).

Churchill Downs has, itself, entered the account wagering business. In April 2006, Churchill Downs entered into an agreement with Magna and Racing UK to form a subscription television channel to broadcast races from Churchill Downs's racetracks, Magna's racetracks, as well as from other North American and international racetracks, to the United Kingdom and Ireland. Newcote Services, Ltd., a Gibraltar-based rebate shop, is one of two account wagering providers with which Racing World, Ltd. has contracted. Churchill Downs Investment Company also holds a 30 percent interest in

North American Simulcast Racing Information Network of NASRIN Services, LLC. Its goal is to interface all racing and simulcasting locations in North America onto a single high-speed network independent of any totalisator system supplier.

In March 2007, Churchill Downs announced that it anticipates launching an advance-deposit wagering platform called www.twinspires.com, providing bettors with a mechanism to wager on racing content owned primarily by Churchill Downs and Magna. At the same time, Churchill Downs acquired a 50 percent interest in HRTV, a horseracing television channel currently owned by Magna. HRTV will distribute the audio-visual signal of its races through cable or satellite to homes for advance deposit wagering. Churchill Downs and Magna also agreed to form a joint venture through which racing content of Churchill Downs and Magna will be made available to racetracks, OTBs, casinos and advance-deposit wagering providers. In addition, this venture will purchase racing content that can be available at Churchill Downs and Magna outlets. Finally, Churchill Downs and Magna agreed to exchange racing content from both entities to make it available for wagering through racetracks, OTBs and advance-deposit wagering providers owned by Churchill Downs and Magna.

Delaware North Companies Gaming and Entertainment, Inc. (Delaware North) has commercial relationships with various offshore rebate shops and simulcasting services. They include Racing and Gaming Services, Inc. (RGS), Youbet.com, TRC/TRNI, and Xpress Bet/MEC (which is owned by Magna and distributes simulcast signals to the United Kingdom, Ireland and Austria). Delaware North also does business with Euro Off-Track Betting. After being named in the *Uvari* indictment, Euro Off-Track Betting, a rebate shop based on the Isle of Man, was barred by the New York State

Racing and Wagering Board. Prior to this, Delaware North's Finger Lakes Racing Association, located in New York, had a commercial relationship with Euro Off-Track Betting. While Finger Lakes ceased doing business with Euro Off-Track Betting, Delaware North's greyhound tracks continue to do business with the company.

Woodbine Entertainment Corp. (Woodbine) has current and past commercial relationships with offshore rebate shops and simulcasting services. Woodbine currently maintains simulcasting agreements with Youbet.com. Youbet, a company which has had its own difficulties in the past (see above) purchased International Racing Group (IRG), an offshore company named in the *Uvari* Indictment. IRG was also, as a result of this indictment, banned by the New York State Racing and Wagering Board. Upon Youbet's purchase of IRG, Woodbine stated that it would not allow IRG to use Woodbine's major thoroughbred and harness racing signals.

Woodbine has also had a number of past relationships with offshore rebate shops and simulcasting services including Grupo Caliente; World Gaming Services, Inc.; and The Racing Network. From 1995 through 1998, Woodbine's predecessor, the Ontario Jockey Club, had a simulcast agreement with Grupo Caliente. According to Woodbine, this relationship was terminated in 1998 after a number of occasions in which it did not receive payment from Grupo Caliente.

In the late 1990s, the Ontario Jockey Club provided a simulcast feed to World Gaming Services, Inc. (WGS), a rebate shop based in Anitgua, West Indies and a wholly owned subsidiary of Starnet Communications International, Inc. based in Vancouver, BC, Canada. Starnet began business in 1996 as a provider of Internet pornography and, in

1997, branched out into gaming and gaming technology. It obtained a gaming license from the Government of Antigua and operated gaming websites through WGS. In April 1997, WGS obtained a simulcast feed from Woodbine Racetrack. In August 1999, the Royal Canadian Mounted Police, together with U.S. Customs and IRS agents, raided Starnet's offices and the homes of its principals, pursuant to an investigation into illegal gambling and child pornography. Starnet moved its offices to Antigua where on-line gambling is legal and sold its adult entertainment business. Woodbine terminated its relationship with WGS and, according to Woodbine, does not do business with the entity.

Woodbine was one of the original partners of The Racing Network (TRN), which was established in 1998 to serve various European markets through offshore rebate shops. TRN's call center was located in the West Indies. In 2001, TRN ceased operations due to insolvency.

Scientific Games Holding Corp. (Scientific Games) currently has a contractual relationship with Youbet.com. In 2004, Scientific Games contracted with Youbet to provide pari-mutuel services, including a centralized wagering network, along with maintenance and security services. The contract amount is \$7 million over its five year term, with an option to renew for another three years. Youbet is the owner of International Racing Group (IRG), a rebate shop banned in New York by the Racing and Wagering Board.

Discrepancies and Omissions in Responses to Questionnaires

As stated above, all key persons and business entities were required to complete extensive integrity questionnaires. Individuals were required to complete and submit a

Key Person Individual Integrity Questionnaire. Business entities were required to complete and submit a Business Entity Integrity Questionnaire.

Perhaps the most significant discrepancy, as set out below, was discovered in Empire's own questionnaire.

The New York Thoroughbred Horsemen's Association (NYTHA) was established in 1988 and currently has more than 5,000 members. Any owner or trainer who is licensed by New York's Racing and Wagering Board and has run a horse within the prior two year period at Aqueduct, Belmont or Saratoga racetracks may become a member. NYTHA describes itself as a non-stock, not-for-profit membership association representing the interests of thoroughbred horse owners and trainers, and their employees in New York. It also provides health and welfare benefits to backstretch workers as well as funds for equine research.

According to NYTHA's questionnaire, it owns an undisclosed number of units in Empire, comprising three percent of the outstanding ownership units. In its questionnaire, NYTHA states that it has a "three percent non-equity interest in Empire Racing Associates, LLC," that it "received in exchange for its exclusive endorsement of Empire Racing to acquire the franchise to operate Aqueduct, Belmont Park and Saratoga." NYTHA endorsed Empire in March 2006 and, one month later, NYTHA Board Members Terence Finley and Charles Reiss were appointed to Empire's Board of Managers. (See the above Special Report from Thacher Associates.)

A significant discrepancy, however, has been revealed between NYTHA's questionnaire response and Empire's response in its own questionnaire. While NYTHA's

response states that its three percent interest in Empire was “received in exchange for its exclusive endorsement of Empire Racing to acquire the franchise...,” Empire’s questionnaire response states that NYTHA made an \$110,054 investment in Empire. Moreover, the Ad Hoc Committee Report issued by the earlier franchise selection committee in February 2007 states that NYTHA made an investment of \$123,098 in Empire, representing three percent of the total ownership units issued by Empire. Also in conflict with Empire’s Questionnaire, Empire’s Operating Agreement dated March 22, 2006, states that NYTHA was admitted as a three percent member in consideration for NYTHA’s endorsement of Empire. It states, too, that NYTHA would not be required to pay for these ownership units.

Furthermore, NYTHA states in its questionnaire that neither it nor any of its affiliates had made any political contributions within the past five years. However, NYTHA’s Political Action Committee or PAC has made significant political contributions to various New York State political candidates during this period of time.

Additional discrepancies were also discovered. For example, one individual, Michael Dubb, failed to disclose his racing or gaming licenses. While not included in his questionnaire, investigation revealed that he was issued a license by the New York State Racing and Wagering Board in February 2005. Another person did not make known that he was the managing director of the corporation, Game Banc, Inc., between 2001 and 2003.

Scientific Games Holding Corp. did not reveal that a recent joint investigation by the FBI, the IRS and the North Carolina State Bureau of Investigation resulted in an October 2006 conviction of Scientific Games Vice President Alan Middleton for state lobbying law violations. Also convicted were North Carolina's Speaker of the House, a former aide to the Speaker, and a member of the state's Lottery Commission. Scientific Games also failed to disclose, as was later discovered by this integrity review, that it was involved in a federal litigation matter involving the company's affiliates. In addition, approximately 100 state litigation matters involving affiliates of Scientific Games were discovered. None of these were disclosed by Scientific Games in its questionnaire. Additional undisclosed domestic and foreign litigation matters pertaining to Scientific Games and its affiliates were revealed in the Key Person questionnaire of Ira Raphaelson, Vice President, Secretary, and General Counsel of Scientific Games since 2006.

According to his questionnaire response, Mr. Raphaelson is a member of Empire's Board of Managers (though he holds no ownership interest) and a member of its Integrity Task Force. In his questionnaire, however, Mr. Raphaelson omitted two items. Raphaelson failed to disclose that he had received a subpoena to testify in a 2003 federal case in Nevada. When asked why he had not included this information in his questionnaire response, Mr. Raphaelson stated that it had "slipped his mind." He stated, too, that as he had not included this information in his gaming license application in New Jersey and Nevada, he would have to amend those applications. He also did not disclose a recent civil lawsuit in which he was named as a defendant.

Legal and Regulatory Issues

Empire has indicated that it will maintain an Integrity Task Force, currently chaired by Daniel Alonso, Esq., which will be led by two independent directors who have no financial interest in racing. In addition, it intends to have a compliance officer at each racetrack facility to ensure that all activities are conducted in compliance with its Code of Ethics and all applicable laws, rules and regulations.

As with the others seeking the franchise, many of Empire's members are business people or companies that are engaged in business ventures and thus are often involved in civil litigation. Records of the Superior Court of Ontario, from 2002 to the present, revealed 55 civil suits in which Woodbine Entertainment Group was either a plaintiff or defendant. Scientific Games (or its affiliates) were involved in approximately 150 federal or state civil actions, as well as numerous regulatory matters for equipment or systems failures or other regulatory violations resulting in fines, costs and corrective actions. While civil litigation and regulatory infractions do not necessarily reflect on the integrity of Empire or its members, legal matters pertaining directly to gaming licenses and operation of casinos are identified below.

Magna Entertainment Corp. and/or its subsidiaries have been ordered to pay fines for various violations of law. For example, under an Order dated July 27, 2006, Magna and a number of its subsidiaries were required to pay a fine of \$15,000 to the Nevada Gaming Commission. Gulfstream Park Racing Association, Inc., owned and operated by Magna, under a Consent Order dated March 9, 2007, agreed to a fine of \$65,000 for underage gambling on the casino floor. Remington Park, Oklahoma, under a Consent Order dated October 19, 2006, and Remington Park, Inc., owned and operated by Magna, agreed to pay a fine of \$2,500 to the Oklahoma Horse Racing Commission for permitting an employee without a gaming occupation license into the gaming facility. Flamboro Downs Holding, Ltd., of Ontario, Canada, also owned and operated by Magna, was initially fined \$100,000 (CDN) in 2004 for failure to comply with certain terms of its

racetrack license. The fine was later reduced to \$25,000 (CDN) and an independent security audit was ordered.

In 2005, Arlington Park Racecourse, owned by Churchill Downs, was charged by the U.S. Department of Housing and Urban Development (HUD) with mistreating backstretch workers by violating fair housing laws, providing inadequate living conditions and discriminating in housing backstretch workers with families. While Arlington Park admitted no wrongdoing, in March 2007 a Consent Decree was issued under which Arlington Park agreed to construct new housing, provide equal housing to backstretch workers with families, and pay \$10,000 in civil penalties and \$160,000 in damages.

According to the questionnaire submitted by Scientific Games' Vice President, Secretary and General Counsel, Scientific Games is currently under investigation by the District Attorney of Wake County, North Carolina for violations of the North Carolina Lobbying Act. As mentioned above, in October 2006 Scientific Games' Vice President was convicted of violating North Carolina's lobbying laws.

In 2004, the IRS initiated an investigation into the financing of a casino-development venture promoted by David S. Cordish, President and Chairman of The Cordish Company, which owns National Development Investors. The Cordish Company had teamed with New York developer Richard Fields (see the Excelsior section of this report) to develop two Florida casinos. The project was to be carried out together with the Seminole Indian Tribe. In return for providing "financial advising," the Cordish Company, through its affiliate Power Plant Entertainment, was to receive approximately

30 percent of the casino's profits for a ten-year period. The deal was to be financed with tax exempt municipal bonds and was described as the first Indian casino project to be subsidized by the American taxpayer. In May 2004, the IRS stated that the deal appeared to violate federal tax law, and initiated an investigation into the use of the tax exempt bonds for such a project.

According to DCJS, based upon the fingerprint cards received from an Empire key person, the FBI identified a record indicating that an Empire key person had been arrested in 2006 and charged with Driving Under the Influence. According to the County Sheriff's Department, the case is still pending. This arrest was not disclosed on the key person's integrity questionnaire.

Judgments, Liens, and Bankruptcies

On September 26, 2005, a judgment in the amount of \$1,100,000 was entered against Richard Simon and Sez Who Thoroughbreds, Inc. in the 11th Judicial Circuit Court in Miami-Dade County, Florida. According to information provided by Empire, Richard Simon, through his Florida-based thoroughbred breeding and training company, Sez Who Thoroughbreds, Inc., currently owns .68 percent of the outstanding units issued by Empire. CIT Group/Equipment Financing, Inc. is the named creditor for this \$1,100,000 judgment, the current status of which is unknown. Records of three federal tax liens between November 5, 2004 and May 23, 2005 in amounts ranging from \$71,373 to \$7,871,373 were also found. These records, however, may all pertain to the same lien.

Political Contributions and Lobbying

As with the other entities seeking the franchise, Empire, as an entity, along with its corporate and individual members and investors have made contributions to various political campaigns in New York State over the years. The contributions have been made to candidates of both political parties, demonstrating no discernable pattern of support. In addition, Empire and its members, like other franchise candidates, have engaged in lobbying state elected officials.

Most significant are the actions of founding, now former, Empire member Jared E. Abbruzzese. Searches conducted of the New York State Board of Elections Campaign Financial Disclosure online database and media databases identified a number of political contributions made by Mr. Abbruzzese to New York State Senate Majority Leader Joseph L. Bruno. For example, January 29, 2007 *Satellite News* article reported that Mr. Abbruzzese contributed more than \$118,000 to a campaign committee controlled by Senator Bruno. Additionally, from November 2, 2000 through November 1, 2006, Mr. Abbruzzese reportedly contributed a total of \$40,000 to the New York Republican State Committee.

In addition, several media articles have reported the close relationship and questionable dealings between Mr. Abbruzzese and Senator Bruno. For example, *The New York Times*, on March 26, 2007, reported that Senator Bruno had reportedly steered \$500,000 in state funds to Mr. Abbruzzese's company, Evident Technologies, and that Mr. Abbruzzese had been subpoenaed in the federal government's criminal investigation into Senator Bruno's business dealings. Mr. Abbruzzese is reportedly under investigation by the New York State Temporary Lobbying Commission for flights he provided on his

aircraft to Senator Bruno. One of these flights had taken Senator Bruno to a fundraiser sponsored by thoroughbred-industry interests in Kentucky.

An article in the *Times Union* (Albany, NY), dated January 19, 2007, entitled “Bruno Trip Included Key Appointee; Member of Panel Responsible for Oversight of NYRA was Member of Senator’s Florida Travel Party,” reported the following: “A member of the state’s racing oversight board was among a small group that accompanied Sen. Joseph L. Bruno last year on a Palm Beach excursion that included two days of golf and a helicopter flight to a South Florida horse track. The trip was largely bankrolled by Jared Abbruzzese, a friend of Senator Bruno’s who has been involved with efforts to win the state’s horse racing franchise. Abbruzzese’s and Bruno’s financial records have been subpoenaed by a federal grand jury, according to knowledgeable sources.”

This same *Times Union* article also noted that an official briefed on the federal investigation said that Bruno and Abbruzzese were accompanied on the Palm Beach trip by Joseph Torani, who is the Senate Republicans’ appointee to the New York Racing Association’s Oversight Committee. The state Lobbying Commission, which has no authority over Senator Bruno’s activities, also is investigating whether Abbruzzese is an unregistered lobbyist, a charge Abbruzzese denies. According to the article, NYRA President Charles Hayward said the Palm Beach trip is troublesome because of the coziness between Senator Bruno and supporters of Empire Racing Associates, which hopes to replace NYRA. Hayward further said he has concerns about what was going on behind the scenes as Friends of New York Racing, a group that included Abbruzzese, had morphed into Empire Racing Associates. Empire officials said Hayward is off base in describing Friends of New York Racing as its forerunner. Timothy Smith, the former

head of Friends of New York Racing, and now an investor in Empire, testified before the Lobbying Commission last year that he once had a one-on-one meeting with Senator Bruno at Abbruzzese's Loudonville (NY) home, which Abbruzzese helped arrange.

An article entitled "Bruno Son Emerges as Key Link in Father's Circle of Connections" in *The New York Times* on January 11, 2007, reported that "[a]s part of their investigation into the business dealings of Senator Bruno, federal authorities are examining a series of land deals involving Kenneth Bruno, who has emerged as a nexus between his father and a wealthy businessman, Jared E. Abbruzzese, whose financial ties to Senator Bruno are under scrutiny." The younger Mr. Bruno reportedly was instrumental in persuading the wife of Jared Abbruzzese to pay \$90,000 for approximately 12 acres on Pond View Way from a partnership involving Senator Bruno, according to an owner of the partnership. Weeks before that November 2004 deal was completed, the article states, a Canadian racetrack owner that had hired Kenneth Bruno as a lobbyist formed an advocacy group with Mr. Abbruzzese that would urge an overhaul of the state's horse racing industry, an issue in which Senator Bruno has been playing a major role [see Thacher Special Report above]. In November 2004, Dove Interests, a company controlled by Mr. Abbruzzese's wife, purchased two parcels totaling 11.4 acres for \$90,000.

According to this January 11, 2007 *New York Times* report, Kenneth Bruno's involvement with the Abbruzzeses represents an important link between Mr. Abbruzzese and Senator Bruno, in part because the son was lobbying for a company allied with Mr. Abbruzzese at the time. Kenneth Bruno resigned as district attorney of Rensselaer County to join the law firm Wilson Elser Moskowitz Edelman and Dicker as a lobbyist in

June 2003. Among the clients he brought to the firm was the Magna Entertainment Corporation. When Kenneth Bruno left the law firm in March 2005, according to the news report, he took Magna with him as a client of his new lobbying firm, Albany Strategies. He ceased lobbying in January 2006 to focus on his law practice. Magna and Mr. Abbruzzese later joined in forming the Empire Racing Associates, a consortium of gambling and racing interests that is bidding to get the New York racing franchise.

An April 2006 Albany *Times Union* article reported that Jared Abbruzzese along with a number of Empire investors gathered at Donald Trump's Florida home with Senator Bruno for a campaign fundraiser, paying \$3,000 per couple and \$2,000 per person to attend. Other Empire members in attendance reportedly were Jeff Perlee, Timothy Smith, Dennis Brida, Marylou Whitney, and representatives of Churchill Downs, Inc.

Scientific Games Holding Corp. (SGC) reportedly also has been investigated for its lobbying activities in other states, according to multiple media sources. For example, several news agencies including the *Associated Press*, reported on the recent investigation of SGC by the FBI, the Internal Revenue Service, and the North Carolina State Bureau of Investigation for possible violations of North Carolina's lobbying laws. Ultimately, six people pleaded or were found guilty as a result of the investigation, including North Carolina State Speaker of the House Jim Black. Kevin Geddings, a public relations executive and member of North Carolina's lottery commission, was found guilty by a federal jury in October 2006 of five counts of mail fraud. Mr. Geddings had failed to disclose more than \$250,000 in payments his public relations firm had received from SGC during its bid for North Carolina's lottery contract. The

indictment against Mr. Geddings outlined a nearly five-year relationship between Mr. Geddings and SGC. Alan Middleton, a former Vice President of SGC, and Meredith Norris, a former aide to Speaker Black, were found guilty in North Carolina State District Court in October 2006 of lobbying-law violations. Speaker Black, who had appointed Mr. Geddings to the lottery commission, resigned from the North Carolina House of Representatives on February 14, 2007, and shortly thereafter pleaded guilty in federal court to corruption-related charges.

The *Denver Post*, in January of 2004, reported on a new policy implemented by the Colorado Lottery Commission barring lottery employees from accepting any gratuities from businesses seeking to win or keep multi-million dollar contracts with the state lottery. At the time, SGC was in competition with Rhode Island-based GTech for Colorado's \$56.2 million lottery contract. SGC eventually won the contract, and its competition with GTech was cited as an example of the problem. According to the article, "During the bid process, employees of both companies regularly entertained Lottery officials" with dinners, tickets or rounds of golf. SGC denied any wrongdoing. It was later reported that a probe by the Colorado Department of Revenue had placed a Lottery Commission contract with SGC on hold until separate criminal and administrative probes could determine whether the deal was crafted fairly. The Colorado Bureau of Investigations reportedly seized twenty-three computers from Lottery offices in an attempt to answer questions about gifts or trips provided by SGC and another company to Lottery officials. Colorado's Lottery director later resigned under pressure. SGC's attorney, Martin E. Schloss, called the probes "pretty garden-variety stuff."

Lastly, searches by the consultants of the New York State Board of Elections Campaign Financial Disclosure online database identified the several New York State campaign donations by Empire. In the fall of 2006, Empire donated \$16,500 to the New York State Senate Republican Campaign Committee and \$8,500 to the State Senate campaign of Joseph Bruno. During the same period, Empire and/or its political action committee donated a total of \$4,500 to the gubernatorial campaign of Eliot Spitzer. Individual or corporate members of Empire have made similar contributions to the New York State Senate Republican Campaign Committee; for example, in 2005 Tim Smith donated a total of \$6,000 to that committee.

EXCELSIOR RACING ASSOCIATES, LLC

Excelsior Racing Associates, LLC (Excelsior) became a Limited Liability Corporation in New York State on June 12, 2006. Its registered address is, c/o Coastal Development LLC, at One East 57th Street, New York, NY 10022. According to Excelsior's Business Entity Integrity Questionnaire (BEIQ), the following entities, all currently inactive, are wholly owned by Excelsior: Excelsior Racing and Entertainment Group, LLC; Excelsior Racing Club, LLC; and Excelsior Jockey Club, LLC.

Key Persons and Business Entities

The ownership structure of Excelsior underwent significant changes in March and April of 2007, with the exact nature of the current ownership structure unknown. The following is a summary of information received by the Inspector General's Office to date regarding the ownership of Excelsior and the resulting designation of key persons and Business Entities.

According to the original BEIQ provided by Excelsior, there were three equity owners: Coastal Development Racing Associates, LLC; SJG New York, LLC; and Alpha Racing Associates I, LLC. Coastal Development Racing Associates is wholly owned by Coastal Triangle Associates, LLC, which is in turn wholly owned by Richard Fields.¹⁴ As to equity owners SJG New York, LLC and Alpha Racing Associates I, LLC, based upon reported changes in the Excelsior team, these equity owners have been replaced. Alpha

¹⁴ Note that according to Fields' KPIQ, Fields wholly owns Coastal Triangle Associates LLC, which, in turn owns 100 percent of Coastal Development Racing Associates, LLC.

Racing Associates I, which was wholly owned by Tishman Speyer, is no longer an equity owner as Tishman Speyer has left the Excelsior Group. SJG New York, LLC was equally owned by Kinsman Racing Club, LLC and Sarabel Racing Club, LLC. Kinsman Racing Club, LLC was equally owned by New York Yankees' owner George Steinbrenner's family members: Harold Steinbrenner; Henry Steinbrenner; Jessica Steinbrenner; Jennifer Steinbrenner; and, her husband, Stephen Swindal. At the end of March 2007, Swindal and the Steinbrenners left the Excelsior group. As a result, Kinsman Racing Club, LLC is no longer believed to be an equity owner of SJG. Sarabel Racing Club, LLC, which is owned by members of the Johnston family, reportedly maintains an equity position in Excelsior, and has submitted a BEIQ, while SJG New York, LLC has not.

After the submission of Excelsior's original BEIQ, additional information emerged regarding changes in its ownership structure. Excelsior's New York State Racing Franchise Proposal Addendum, dated March 31, 2007, states that the Excelsior "team members" consist of Richard Fields/Coastal Development LLC, the Johnston Family (William Johnston Jr., John A. Johnston, William Johnston III) and William Mulrow. On April 10, 2007, Excelsior's attorneys informed the Inspector General's Office that Excelsior was adding three new key persons to its group: Stephen Wynn, Steven Roth (and Vornado Realty Trust), and Richard Bronson.

Stephen Wynn had reportedly been part of Thoroughbred Racing-NY, a group that entered the process late, only to withdraw early on. Mr. Wynn's ownership interest in Excelsior is through a number of his companies. According to the BEIQ executed by Wynn Resorts, Ltd. (Wynn Resorts), Stephen Wynn currently holds a 24.33 percent

ownership interest of that entity. Wynn Resorts is a developer and owner of destination casino resorts, operated through wholly-owned subsidiaries. Mr. Kazuo Okada also owns 24.33 percent of Wynn Resorts through his company Aruze USA. The remaining 51.34 percent of the company is publicly traded. Mr. Wynn disclosed in his Key Person Integrity Questionnaire that Wynn Resorts' wholly-owned subsidiary LRW Development LLC is a member of, and owns, 33 percent of Triple S LLC, which, in turn, owns 50 percent of Excelsior.

Steven Roth's ownership interest in Excelsior is through his ownership, along with Michael D. Fascitelli, of ABS Racing LLC. ABS Racing holds a 16.6 percent ownership interest in Excelsior; Roth and Fascitelli each hold an 8.3 percent ownership interest in Excelsior through their respective ownership interests in ABS Racing. ABS Racing was incorporated on April 6, 2007 as a "special-purpose entity which will own a percentage interest in the joint venture entity bidding on the license to operate the New York Racing Association." Roth is the Chairman and Chief Executive Officer of Vornado Realty Trust, Inc., a publicly traded, fully-integrated real estate investment trust operating primarily in the New York, New Jersey and Washington, D.C. metropolitan areas. He owns ten percent of Vornado's outstanding shares. Michael Fascitelli is Vornado's President and Trustee.

An amended BEIQ for Excelsior detailing its new ownership structure has not been received. Through interviews, however, a picture of Excelsior's ownership structure has emerged.

Mr. Fascitelli stated that the combination of his and Steve Roth's knowledge of real estate, with Stephen Wynn and Richard Bronson's gaming experience, created a strong team to bid for the franchise. Mr. Fascitelli explained that he and Mr. Roth are investing personally in this venture because they "thought this was a gaming-driven investment," and, given the many restrictions placed on real estate investment trusts, Vornado Realty Trust has not entered the gaming business. He noted that he and Mr. Roth brought this venture to the attention of Vornado's board, and that they will offer Vornado any real estate opportunities that may arise as a result of the bid. As to his ownership interest in Excelsior, Mr. Fascitelli explained that ABS Racing, Stephen Wynn, and Richard Bronson each currently owns one-third of 50 percent of Excelsior, but that these percentages may change upon the formation of a new limited liability company in the future.

Mr. Bronson described Excelsior's ownership as 50 percent Fields/Coastal and 50 percent Triple S, comprised of Messrs. Wynn, Bronson, and Roth. Jeremy Kleiman, Esq. told the consultants during the interview of William Johnston, III that the Fields/Johnston family/Mulrow team would collectively have 50 percent ownership in Excelsior, which would be broken down with Fields having 35 percent, the Johnston family 10 percent, and Mulrow 5 percent. William Johnston, Jr. later telephoned the consultants to correct Mr. Kleiman, whom he described as "Fields's lawyer." Mr. Johnston advised that nothing has been decided with respect to the Fields/Johnston family/Mulrow split, and their percentages of ownership were still in a state of flux.

Excelsior's Advisory Board has also undergone changes since its original proposal submission. Most recently, Excelsior reported that its Advisory Board consists

of the following individuals: Jerry Bailey, Dr. Jerry Bilinski, Gary Contessa, R. Wayne Diesel, Rev. Floyd Flake, Amaziah “Bill” Howell and Marion Trieste. Excelsior’s original proposal designated as “teammates” the following: William Mulrow; Citigroup Global Capital Markets; Goldman Sachs; Latham and Watkins, LLP; and Boies, Schiller and Flexner, LLP. Excelsior’s Proposal Addendum changed this list of teammates to include Citigroup and SafirRosetti.

Additionally, Excelsior’s bid proposal addendum states that Excelsior added a Gaming Compliance Team consisting of the following individuals: James Darcy, Timothy McNally, Philip C. Parenti, and Thomas Sheer. Only Philip Parenti was previously identified in Excelsior’s BEIQ as a gaming consultant.

Pursuant to this integrity review, Excelsior identified its key persons and Business Entities. Excelsior’s key persons are Richard Bronson, Richard Fields, William Johnston Jr., John A. Johnston, William Johnston III, William Mulrow, Steve Roth (and/or Vornado Realty), Michael D. Fascitelli, and Stephen Wynn. Its Business Entities are Coastal Development, LLC; Coastal Development Racing Associates, LLC; and Sarabel Racing Club, LLC. Furthermore, others involved with Excelsior are identified as Persons of Interest; they include Jerry Bailey; Gerald “Jerry” Bilinski, D.V.M.; Gary Contessa; R. Wayne Diesel; Reverend Floyd H. Flake; Amaziah “Bill” Howell; Philip C. Parenti; and Marion Trieste.

According to Excelsior’s BEIQ, provided before the new ownership interests joined Excelsior, its sole bank account is a checking account held with Chase Bank. It has no employees and has paid no compensation to any associated individual. It has no

office space, equipment or real estate, and its address is that of a business entity controlled by Richard Fields. Excelsior's original capital investment, as described in its BEIQ, consisted of \$960,000 provided by Coastal Development Racing Associates, LLC (\$600,000); SJG New York LLC (\$200,000); and Alpha Racing Associates I, LLC (\$160,000). An additional capital investment of \$2,240,000 was reported to be comprised of \$920,000 from SJG New York, LLC and \$1,320,000 from Coastal Development Racing Associates, LLC, for a total capitalization of \$3,200,000.

Following are the results of the integrity review in regard to Excelsior, its business entities, and its key persons. As in the case of the other entities, only significant or adverse information is reported herein.

Affiliations with Rebate Shops

The issue of rebate shops and the measures Excelsior will take to ensure the integrity of racing in New York should it receive the franchise was explored. As discussed above, rebate shops are a serious concern because they can serve as conduits for illegal activities, such as money laundering, and may be associated with race fixing and horse doping.

In his interview, William Johnston Jr. said that he did not ban rebate shops from the tracks he operated, which include Balmoral Park and Maywood Park in Illinois, but rather attempts to ensure that they comply with the law. He explained that he has met with the Illinois Attorney General and the Illinois Racing Board to determine what can be done about regulating offshore betting. Nonetheless, he conceded that it is difficult to trace bets coming out of the rebate shop hubs, and that he partially relied on a totalisator

company, Scientific Games (as discussed above, a company with its own checkered history), to regulate rebate shop bets for his tracks. He stated that sometimes the totalisator companies move a bet from one hub to another and that it is difficult to trace the bet back to its point of origin. Johnston also stated that he led the fight to put blood/gas testing machines at racetracks to combat horse drugging.

When questioned about simulcasting contracts, including any involving Grupo Caliente, Johnston referred the consultants to Jim Hannon, who oversees simulcasting for Johnston's racetracks. Hannon stated that two of Johnston's tracks, Maywood and Balmoral Park, simulcast to a San Diego, California company, MIR International, which does business with Hippodrome de Caliente (i.e., Grupo Caliente), a race track in Tijuana, Mexico. MIR International is Arturo Alemany Salazar's company. As mentioned above, Salazar is Grupo Caliente's U.S. representative for simulcasting events in the United States and Mexico. According to Hannon, Balmoral and Maywood only send their TV signal to MIR, and receive a daily flat fee for the transmission. Again, according to Hannon, they purportedly do not co-mingle any racing bets with MIR, which creates its own betting pools.

Hannon further stated that Maywood and Balmoral have simulcasting contracts with a number of offshore and international locations: in Austria through a contract with Magna Entertainment; Racing and Gaming Services (RSG) in St. Kitts; Euro Off Track on the Isle of Man; International Racing and Gaming (IRG), formerly of Curaçao, which was recently purchased by Youbet.com, a California company; and a joint venture of over 100 companies representing 600 betting outlets in Canada. Hannon advised that the contracts with the offshore entities contain clauses which prohibit the entities from

providing rebates to Illinois customers and prohibit them from taking wagers from Illinois residents.

Of note, however, is that three of the aforementioned rebate shops were banned in 2005 by NYRA, and that the New York State Racing and Wagering Board prohibited New York tracks from entering into contracts with them for simulcast services in order to “maintain the integrity of all New York State Thoroughbred and harness racing and pari-mutuel wagering.” Although the Racing and Wagering Board later lifted the ban on Racing and Gaming Services, the prohibition remains in place in regard to the other two.

Mr. Hannon was aware that Euro Off Track was named in the *Uvari* Indictment as a rebate shop through which various criminal activities allegedly occurred. He stated that, in response to the indictment, Maywood and Balmoral initially removed Euro Off Track from its simulcasting lists. After consultation with Standardbred Investigative Services (SIS), the racetracks’ investigative group, and concluding that the offshore entity was not offering rebates to Balmoral and Maywood customers, Euro Off Track was reinstated. Hannon further stated that, in general, they rely on SIS and the totalisator companies to help identify the sources of wagers, and on SIS to evaluate whether offshore entities are operating lawfully. Franklin Fabian, the President of SIS, was contacted to obtain current information about Euro Off Track, now called European Wagering Services. However, Mr. Fabian declined to provide the information citing client confidentiality illustrating the very difficulty in assessing the integrity of rebate shops and their clients.

In general, while the Johnstons state that they are concerned about the integrity of the operations of their race tracks, they continue to do business with those who may otherwise be involved in illicit activities. For example, while Euro Off Track may not have offered rebates to Illinois residents, the lawfulness of its other activities does not appear to have been addressed. This is especially noteworthy in that Euro Off Track is still banned from simulcasting New York races. Doing business with rebate shops such as Euro Off Track as well as Grupo Caliente would certainly seem to require the utmost scrutiny.

Two members of Excelsior, Steven Roth and Richard Fields, have ownership interests in Suffolk Downs thoroughbred racetrack in Boston, Massachusetts. As of March 30, 2007, Richard Fields owned 39.6 percent, and controlled an additional 4%, of Sterling Suffolk Racecourse, LLC, which owns and operates Suffolk Downs. In 2005 Vornado acquired a 21 percent interest in Sterling Suffolk through a wholly-owned subsidiary, Vornado Suffolk, LLC. Steven Roth owns ten percent of Vornado Realty Trust and is its Chairman and CEO, and Michael Fascitelli is Vornado's President. According to Mr. Roth, this interest is currently valued at over \$11 million. Mr. Fascitelli described Vornado's role on Suffolk Downs's board as being limited to real estate planning and to assuming the role of "savvy businessman." Mr. Fascitelli advised the consultants that Vornado had recently helped the track restructure a loan.

Although occurring prior to Mr. Roth's and Mr. Fields' ownership of Suffolk Downs, the track has had a history of organized crime-related activities. According to media sources, Tony Ciulla, a former member of, and master race-fixer for, Boston's

infamous Winter Hill Gang, has testified in a racketeering trial against seven associates in connection with their involvement in a “multimillion-dollar race-fixing scam at Suffolk Downs and several other East Coast tracks” in the 1970s. The alleged organized crime figures against whom Mr. Ciulla testified included James “Whitey” Bulger, Stephen “The Rifleman” Flemmi, John Martorano, and Francis “Cadillac Frank” Salemme.

More recently, according to media sources, in 2004 the Massachusetts Racing Commission granted Burton Sipp a license to train horses, and since that time, Mr. Sipp has been training horses at Suffolk Downs. Massachusetts granted the license to Sipp despite an extensive history of bans and violations in his 30-year career, including a 1986 witness tampering conviction in New Jersey to satisfy an indictment for fraud in connection with allegations that he destroyed horses to collect inflated insurance claims. In 1990 Sipp was indicted in New Jersey for deceptive business practices and attempted theft by deception, arising from allegations that he staged a burglary at his pet store to collect insurance for allegedly stolen exotic birds. Sipp returned the money and the charges were dismissed. In 1994, the Penn National Track refused to allow Sipp to race, despite his having been granted a license by the Pennsylvania Horse Racing Commission. A court upheld the track’s refusal, stating: “In light of Sipp’s extensive record, a reasonable mind could readily conclude that Sipp’s association with horse racing not only taints the image of that industry but also fosters a tawdry image of that industry.” In 1998, Sipp agreed never to apply for a license or do anything that would require licensing in New Jersey as part of a deal to resolve allegations that he had trained horses in New Jersey in 1994 under another trainer’s name. Although a New Jersey judge reportedly

once described Sipp as “a man whose lack of integrity is unimpeachable,” Sipp trains horses at Suffolk Downs.

According to documents provided by Excelsior, it is apparent that Sterling Suffolk Downs, LLC, the operator of Suffolk Downs racetrack, maintains contractual relationships with numerous offshore entities located in places such as Mexico, the Bahamas, Venezuela, and Jamaica. According to these documents, Sterling Suffolk Downs has contractual relationships with rebate shops that include several of the NYRA Ten, including Euro-Off Track, Tonkawa Indian Reservation (through Las Vegas Dissemination Company), Elite Turf Club (through Las Vegas Dissemination Company), Lakes Region Greyhound Park (now known as the Lodge at Belmont), Coeur d’Alene Casino (through Lewiston Raceways, Inc.), and Racing and Gaming Services (through Stevenson and Associates).¹⁵ In 2005, Sterling Suffolk Downs had a contractual relationship with Excelsior Casino, another of the NYRA Ten. Sterling also has contractual relationships with the following offshore rebate shops and simulcasting services: Grupo Caliente (through MIR International Services, Inc.); AmericaTab; The Racing Channel, Inc./The Racing Network International; and Youbet.com, Inc. (through Youbet Oregon).

Its relationship with Youbet.com (Youbet) requires further comment. According to media sources, in February 1999, Sterling Suffolk Downs entered into an agreement with Youbet to offer live on-line racing and betting from Suffolk Downs racetrack.

¹⁵ As noted above, The Lodge at Belmont and Racing and Gaming Services are no longer banned from doing business in New York.

Suffolk Downs is currently listed as a “partner track” on Youbet’s website.¹⁶ Youbet is a provider of technology and pari-mutuel horseracing content through Internet and telephone platforms. It also supplies totalisator systems, terminals and other pari-mutuel wagering services and systems to the pari-mutuel industry through its subsidiary, United Tote. Youbet’s website offers members the ability to watch and, in most states, wager on horse races. International Racing Group, Inc. (IRG), a subsidiary of Youbet based in Curaçao, Netherlands, Antilles, is an offshore rebate shop.

There are a number of potential criminal and regulatory issues related to both Youbet and IRG. IRG was one of the offshore rebate shops named in the *Uvari* Indictment which, as discussed above, charged 17 defendants, including alleged associates of the Gambino crime family, with operating an illegal gambling business, conspiracy, money laundering, violations of the Wire Act, extortion, wire fraud, and horse doping. IRG is one of the NYRA Ten and is currently banned by Racing and Wagering from doing business in New York. Youbet has been investigated by the Los Angeles District Attorney’s Office for illegal gambling activities. A 1999 Cox News Media Service reported that police had raided the Los Angeles offices of Youbet in October 1999. According to a 2000 *E-Commerce Times* article, Youbet agreed to pay \$1.3 million to California authorities to settle an investigation into its on-line horse-racing operation in the state. The article also reported that the company would pay a \$600,000 civil fine, donate \$500,000 to charitable causes and reimburse Los Angeles

¹⁶ Youbet also conducts business with Churchill Downs, Inc., Delaware North Companies Gaming & Entertainment, Inc., Woodbine Entertainment Group, and Scientific Games Holding Corp., each of which is a member of Empire Racing Associates, LLC and is discussed in the Empire portion of this report.

County for more than \$200,000 in costs associated with the inquiry. Youbet also reportedly agreed to refrain from conducting business with any California resident, although it would be allowed to maintain its operation in the state. In exchange, California agreed not to pursue criminal charges against Youbet or its officers.

Youbet's activities in Minnesota were recently questioned by state regulatory authorities. According to a 2005 article in the *Star Tribune*, the Minnesota Racing Commission and the Minnesota Department of Public Safety's Alcohol and Gambling Enforcement Division sent a letter to Youbet advising it that Internet wagering was illegal in Minnesota. The Executive Director of the Commission pointed out that Youbet responded that Minnesota cannot interfere with an activity that is legal at the federal level. However, a 2006 article on Bloodhorse.com indicates that during a U.S. House of Representatives Judiciary Committee hearing, Michigan Representative John Conyers Jr. stated that Youbet was, at that time, operating despite a cease-and-desist order from the United States Attorney General.

Suffolk Downs also signed a contract in 1998, permitting TVG, a subsidiary of Gemstar-TV Guide International, Inc., to broadcast races from the racecourse and accept telephone wagers on those races. Because the Commonwealth of Massachusetts did not permit telephone wagers at the time, the deal meant that Suffolk Downs would derive only "a small revenue stream" from out-of-state bets on its races. According to media sources, Suffolk Downs signed the deal anticipating that if Massachusetts legalized such wagers in the future, the contract with TVG would put it in a strong position to attract in-home betting, and that in June 2002, TVG exercised a warrant to purchase approximately 16 percent of Youbet common stock. It has also been reported that TVG holds a warrant

which, if exercised, would enable TVG to purchase an additional 51 percent of Youbet common stock.

In approximately July 2002, Suffolk Downs began offering account wagering through both Xpressbet and TVG. Xpressbet, a competitor of TVG, is a subsidiary of Magna Entertainment Corp. (of bidder Empire Racing Associates). In conjunction with Horseracing TV, another Magna Entertainment Corp. subsidiary that provides live coverage of horse racing, Xpressbet provides on-line and telephone account wagering.

Richard Fields, who reportedly owns between 40 and 50 percent of Suffolk Downs, stated that he is opposed to offshore gambling. He also said that the technology is now sophisticated enough to trace the origins of bets to determine if they are coming from offshore gambling locations. Fields emphasized the importance of integrity and that there are two retired FBI agents who presently work for one of his companies and are advising Excelsior. Following the interview, Excelsior submitted a Proposal Addendum which included a section on "Assuring Integrity." The proposal did not include banning simulcast signals to all rebate shops, but to "those that do not provide all necessary information to confirm they operate in a lawful manner."

Discrepancies and Omissions in Responses to Questionnaires

While a comparison of Excelsior's response to the BEIQ and the consultant's review of Excelsior's checking accounts revealed a number of discrepancies, their specific significance has not been determined. Although the total amount of capitalization outlined by Excelsior's BEIQ equals the total amount identified through the account review, the sequence and individual capital contribution amounts are not clearly

presented in the BEIQ. Total capital contributed to Excelsior in 2006 was \$1,920,000. Both Coastal's and SJG's additional contribution amounts were made in several separate instalments and made months apart. Alpha Racing Associates I, LLC's initial capital contribution of \$160,000 was made on February 15, 2007, a month after Excelsior and SJG had made all of their additional capital contributions.

There were other instances in which Excelsior's key persons failed to disclose requested information, including failures to disclose civil litigation, as well as discrepancies regarding political contributions. One individual failed to report approximately \$50,000 in contributions to various political entities in New York State and on a federal level. There were also several discrepancies involving reported business affiliations and those identified through either on-line public records research or tax returns provided by the individuals.

Discrepancies in Richard Bronson's reported suitability of licensing are noteworthy as they pertain specifically to gaming licenses. Mr. Bronson claimed in his KPIQ, and continues to claim, that he has been found suitable for licensing in Nevada, New Jersey and Mississippi. In addition, in his key person interview he reported that he was licensed in the state of California, a venue not disclosed in his KPIQ. This investigation was only able to confirm his suitability for licensing in Mississippi. Although the Nevada Gaming Commission did have a record of Mr. Bronson in its computer, it was unable to confirm that he was found suitable for a license. The New Jersey Casino Control Commission and the California Gambling Control Commission reported that they have no record of Mr. Bronson.

Another inconsistency between an Excelsior key person's questionnaire response and a record check occurred when the Division of Criminal Justice Services reported the results of criminal history checks. Despite his negative responses to the criminal history section of the KPIQ, a fingerprint-based criminal history report revealed that he was recently arrested and charged with Driving While Under the Influence of Alcohol (DUI). Although the DUI case apparently resulted in a not guilty disposition in 2005, the failure to report it is noted.

Legal and Regulatory Issues

Similar to the other entities seeking the racing franchise, many of Excelsior's members are business people involved in numerous high-level ventures and, consequently, are frequently involved in civil litigation. Vornado Realty Trust has been sued numerous times, most of which are personal injury claims or employment-related

matters. The Excelsior members who are not in business have held positions that by their natures subjected them to lawsuits (e.g., head of a government agency). While civil litigation should not, in itself, call into question the integrity of Excelsior or its members, there are a number of instances in which the substance of the litigation is material because it involved racing/gaming, or pertained to allegations of fraud or business-related misconduct.

Stephen Wynn is the defendant in three labor lawsuits filed in Nevada's Clark County District Court in 2006 and 2007. One case was filed as a class-action complaint on behalf of 500 casino dealers. According to a 2006 *Wall Street Journal* article, Wynn changed a casino's tipping policy so that supervisors would share the tips because they were making lower salaries than their dealers. This led to protests, several lawsuits, and a complaint filed with the National Labor Relations Board (NLRB). Additionally, in January 2007, the NLRB issued a complaint notifying Stephen Wynn and six managers of Wynn Las Vegas that they had been accused by employees of threatening them with job losses and reduced income if they joined a union or protested the changes to the casino's tipping policies.

A 2005 article in *The Record* reported the settlement of a shareholder lawsuit against Steven Roth; Michael Fascitelli; Vornado Realty Trust; Vornado Realty, LP; Vornado Operating Company and others in Chancery Court in Delaware. The plaintiffs asserted Vornado Operating Co. violated Delaware law by not seeking voter approval before selling its stake in AmeriCold Logistics to a Vornado Realty Trust-controlled partnership for more than \$28 million. The lawsuit further alleged that the operating company received less for the sale than it would have on the open market and that "Vornado ultimately crippled the operating company by allowing it to participate in only one venture 'and sucking all the profits (and more) out in rent.'" According to the news

story in March 2005, the court approved a settlement pursuant to which Vornado Realty Trust paid approximately \$4.5 million to shareholders of Vornado Operating Co.

Vornado's most recent 10K filing with the SEC revealed a lawsuit, *Pentagon Plaza Inc., et al. v. H Street Building Corp., et al.*, filed in 2005 in the Superior Court of the District of Columbia. The plaintiffs alleged that Vornado encouraged H Street and the other defendants to breach their fiduciary duties to the plaintiffs, and interfered with prospective business and contractual relationships. The suit was dismissed in April 2007.

Jerry Bilinski, D.V.M. has been the subject of an investigation by the Office of the State Inspector General. Concluding its 1996 investigation, the Inspector General's Office found that as Chairman of the New York State Racing and Wagering Board, Jerry Bilinski had made two out-of-state trips that he claimed were for state business but were, in fact, personal in nature. Bilinski was required to make restitution to the state for his misuse of state funds. During the course of the investigation, he resigned from the Racing and Wagering Board. Compounding this 1996 finding that Bilinski misappropriated state funds is his apparent recent attempt to obfuscate the facts surrounding the matter.

When interviewed for this review, Bilinski stated that he and Senator Joseph Bruno took this trip to Florida in 1995 to meet with horsemen to find out what they were doing and to get new ideas on racing. Although it was determined that the trip was not for business purposes, Bilinski said that while he disagreed with the finding, he still

reimbursed the Racing and Wagering Board \$800 for the cost of the airline ticket. A review of the Inspector General's report clearly contradicts Bilinski's characterization of the trip as business-related, and determined that the trip was taken with his friend James Towne, not with Senator Bruno as Bilinski now claims.

Bilinski stated to investigators in 1996 that one business-related activity was a bus tour to the Seminole Reservation to observe gaming operations there. However, James Towne, Bilinski's travel companion, told investigators that the visit was his idea and the purpose was simply a sightseeing excursion to the surrounding Everglades. Toward the end of Bilinski's 1996 interview with the Inspector General's Office, he admitted that this outing could not be justified as a state expense. Bilinski also claimed that his day at Gulfstream Park was business-related. However, the Inspector General's investigation established that, except for a brief chance encounter with the track's director, his day's activities consisted of nothing more than what any individual would do enjoying a day at the races.

The Inspector General's report also revealed that Bilinski neglected to mention in his interview that there was a second purported business trip (to Louisville for the Kentucky Derby) which was likewise found by the Inspector General to have been for personal reasons, and not business-related.

Stephen Wynn was asked about a 1986 New Jersey license hearing regarding the Golden Nugget, which Wynn owned until its sale to MGM in 1990. At the hearing, the Division of Gaming Enforcement stated that certain Golden Nugget "marketing or junket representatives have been hired who have been the subject of, and in some cases the

object of formal action by gaming regulators and the law enforcement community.” Mr. Wynn commented specifically about Mel Harris, a focus of the hearing. He said that Harris had not been truthful with the Golden Nugget about his having met Anthony “Fat Tony” Salerno (former head of the Genovese crime family). When Mr. Wynn found out that Harris had met Salerno, he stated that he terminated his relationship with Harris that same day.

Mr. Wynn was questioned about his 2004 application to the Nevada Gaming Control Board for Wynn Las Vegas, in which he disclosed that “in February 1982, the Gaming Board for Great Britain questioned me regarding Golden Nugget Inc.’s application for a Certificate of Consent to operate a casino in London, England. The application was ultimately denied. No reason was given for the board’s refusal. However, it is believed that a significant issue related to the degree of control the company was willing to vest to British residents.” Mr. Wynn discussed the concerns raised by the British over foreign ownership, but he also said that Scotland Yard set up a special branch to “dig up dirt” on him that produced a report saying he was a “front man for the Genovese family.” This branch was later dissolved and the two authors of the report were fired, according to a Scotland Yard commander who testified about this in a later proceeding.

Judgments, Liens, and Bankruptcies

Richard Fields is named as the debtor in ten liens and judgments. The amounts involved range from \$2,209.87 to \$292,041.72, and were filed from 1987 to 2004. Although no bankruptcy records were located naming Fields, in his amended KPIQ, he

disclosed that an entity with which he was associated, Catch a Rising Star, Inc., had filed for bankruptcy.

Four judgments and liens were filed naming Amaziah Howell between 1995 and 2006. All list Howell as a debtor and the amounts range from \$881 to \$321,471. The \$321,471 judgment was filed in 2005; the creditor being Community Capital Bank. The status of this judgment was not available.

The consultants identified several judgments filed nationwide in which Vornado Realty is named as the debtor. For example, there is a \$302,872 judgment filed in 1999 in the County Clerk's office in Nassau County, New York, which, according to the consultant's on-line research, has not been satisfied. While a number of the judgments have been satisfied, the status of others remain unclear. Vornado Realty has also been the subject of state tax liens, but these have all been released, according to records identified by the consultants. Steven Roth's personal credit report cited no bankruptcies, collections, civil litigation or late payments (either current or historical).

The consultant's review of Mr. Wynn's Experian credit report revealed no bankruptcies or current delinquent accounts. Although a state tax lien was reported, it had been satisfied.

Other individuals involved with Excelsior have had debtor judgments and/or bankruptcy filings; however, the debts were relatively small and the bankruptcy filings occurred more than ten years ago and have since been discharged.

Political Contributions and Lobbying

As with the other groups seeking the racing franchise, Excelsior's members have made contributions to political candidates and to political organizations of both parties in New York State. Similarly, a number of lobbyists have been retained in relation to the racing franchise process. Certain of the more significant contributions or political connections are set out below.

Richard Fields has been interviewed several times regarding campaign contributions and jet flights that he had provided, through his business entities, to then-Attorney General Eliot Spitzer and then-Senate Minority Leader David Paterson. The New York State Temporary Commission on Lobbying has reportedly made at least three separate inquiries in reference to flights provided to then-candidates Spitzer and Paterson by Fields through his business entities ES Aviation, LLC and Coastal Development Aviation, LLC. The inquiries occurred in January 2007, June 2006 and February 2006. These involved, respectively, flights connected to a Spitzer for Governor fund raising event in Wyoming, air travel provided to Eliot Spitzer to three different U.S. cities in May 2006, and air travel by David Paterson. The inquiry regarding then-Senator Paterson resulted in a settlement in which Fields agreed to pay \$9,000 to the Lobbying Commission. Eliot Spitzer's gubernatorial campaign committee paid \$103,871 to companies owned by Richard Fields for funds expended on the campaign's behalf. SG Management was paid \$52,579 for catering and other costs related to a Wyoming campaign event and Coastal Development was paid \$51,292 for transportation.

In his key person interview, Richard Fields stated that nothing improper was done regarding the use of the planes. He said he has established a protocol, with the assistance

of attorneys versed in state and federal regulations, governing the use of the plane by state or federal officials or political candidates. The trips taken by then-Senator Paterson and then-gubernatorial candidate Spitzer had been approved through this protocol.

Media reports indicated that Richard Fields lobbied New York State on behalf of the Wisconsin Oneida Tribe for approval for the tribe to build a casino. According to these reports, Richard Fields's company, Power Plant Entertainment, LLC, was a registered lobbyist in Albany. The tribe has also sued the state to secure what it claims as its ancestral land in New York and hired a top Albany lobbying firm which employed Kenneth Bruno, the son of Senate Majority Leader Joseph Bruno.

In addition, a 2004 article in the *Baltimore Sun* noted that Richard Fields and/or his companies have contributed tens of thousands of dollars to political candidates and political committees in Florida and other key gambling states. The companies cited were Coastal Development, LLC and Power Plant Entertainment, LLC. According to a 2006 *Miami Herald* article, Fields and Coastal Development made contributions to now Governor Charlie Crist's Gubernatorial campaign. Governor Crist will reportedly have the final say in the contract the state would have to sign with the Seminole and Miccosukee tribes before they are allowed to expand their gaming operations to bring slot machines to Broward County, Florida.

News reports have written that William Mulrow maintains a close relationship with Governor Eliot Spitzer, including a claim that Mr. Mulrow's and Governor Spitzer's families vacationed together in Ireland. In his interview with consultants, Mr. Mulrow stated that with respect to his relationship with Governor Spitzer, he has known him since

1994 and that they have had much interaction as a result of the political campaigns in which they have been involved. Mr. Mulrow further explained that while he and Governor Spitzer did take a trip together to Ireland, it was a group trip that included over thirty people as part of the New York Friends for Ireland. Mr. Mulrow took the trip with his daughter, and his interaction with the Governor was always part of the larger group. Mulrow said he has never been to Eliot Spitzer's home and never had breakfast, lunch, or dinner with him. Mulrow stated that while he attended an inaugural event at the Governor's mansion, he has not seen the Governor since the inauguration nor has he helped him financially. When asked, Mulrow stated that he has not had a conversation with Governor Spitzer about the Excelsior proposal, and could not recall whether he mentioned that Excelsior would be resubmitting a franchise proposal. Mulrow also could not recall if he had spoken to anyone on Governor Spitzer's staff about the Excelsior bid.

Other members of the Excelsior team or their companies have made political contributions to New York State Senate Majority Leader Joseph Bruno's campaigns or to the New York State Senate Republican Campaign Committee. Between 2002 and 2007, for example, Steven Roth donated approximately \$105,000 to the State Senate Republican Campaign Committee, while also contributing about \$50,000 to the Spitzer-Paterson gubernatorial campaign.

In 2000, the Federal Election Commission (FEC) conducted an investigation of then-New Jersey Senator William Gormley regarding political fundraising activities by Trump Hotels and Casino Resorts, Mirage Casinos, and Harrah's Entertainment. Stephen Wynn stated that he was questioned regarding his involvement in organizing a political fundraising event at Le Cirque restaurant in Las Vegas. News articles said Senator

Gormley received \$40,000 for his campaign at the fundraiser. The articles noted that, at the time, Gormley was championing efforts to spend more than \$200 million to subsidize the opening of a Wynn casino in Atlantic City, New Jersey. An FEC press release reported that, in February 2005, the agency entered into conciliation agreements with Atlantic City Showboat, Inc., Marina Associates, Herbert Wolfe and David Jonas; Gormley for Senate Primary Election Fund; and Mirage Resorts settling the FEC violations. The conciliation agreements resulted in total civil penalties of \$115,000. The Mirage casino was responsible for \$40,000 of the penalty, while the Gormley committee was responsible for \$22,000 and Showboat, Marina, David Jonas and Herbert Wolfe were jointly and severally responsible for \$53,000 of the penalty. Richard Bronson of Excelsior reportedly was a director of Mirage Resorts and president of New City Development, a subsidiary of Mirage Resorts at the time the fine was levied.

Media Reports

Numerous media references were identified regarding Richard Fields's involvement in the Excelsior bid. According to the *Times Union* (Albany, NY), Empire Racing Associates submitted a letter to the executive director of the Ad Hoc Committee on the Future of Racing on December 7, 2006, suggesting that Excelsior might have violated bidding rules and state laws with its use of politically connected representatives and lobbyists in its bid for the New York State racing license. Empire Racing reportedly asked whether Excelsior disclosed that its team included lobbyist William Powers, former top Assembly lawyer Michael Boxley, racing consultant Richard Powell and veterinarian Jerry Bilinski. Empire Vice President Justin McDonald reportedly wrote that such disclosures were required in the bid document. McDonald also reportedly questioned

why no lobbyists for Excelsior or Richard Fields are registered with the Temporary State Commission on Lobbying. Ad Hoc Committee executive director Robert Williams reportedly stated that he was reviewing the letter from Empire, and that some of the people listed by Empire in the letter were named in the Excelsior bid, but that only people who helped put the bid together had to be identified. Excelsior responded that it did not violate any laws or requirements.

While not an adverse media report, an April 3, 2007 article in the *Boston Globe* is relevant. Richard Fields reportedly purchased the largest ownership interest in Sterling Suffolk Racecourse, LLC, the company that runs Suffolk Downs racetrack and which is in competition with the New York tracks. Neither the price nor the percentage of the ownership interest was disclosed, but an executive briefed on the deal said, “Fields bought between 40 and 50 percent.” Fields reportedly wished to revamp the venue into “a modern entertainment complex that would include shops, restaurants, live entertainment, family activities, and – if state government embraces it – casino gambling.” Fields joined the other shareholders of Suffolk Downs, partnerships controlled by local concessionaire Joe O’Donnell, New York retail developer Vornado Realty Trust,¹⁷ and Hall Properties Inc. of Boston. A *Boston Herald* article, dated December 20, 2006, reported that Fields reportedly made a recent bid that valued the track in the \$100 million range. While Excelsior’s bid for the New York State thoroughbred racing license is described as a large deal, Suffolk Downs “could be even

¹⁷ Note that Vornado Realty Trust was recently added as a Key Person of Excelsior Racing Associates, LLC.

more of a gold mine.” The article further stated that while it is expected that if Fields gets Suffolk Downs he will revamp it, no mention has yet been made of slot-machines.

A story reported in the media in 2001 is noteworthy regarding Vornado Realty’s dealings with the Port Authority of New York and New Jersey (the PA), which in February of 2001 had awarded Vornado a 99-year lease to operate the World Trade Center. Vornado’s winning bid of \$3.25 billion was only \$5 million more than the second place bidder, Silverstein Properties Inc. The PA gave Vornado a “20-day exclusive negotiating period” to execute a contract, but, according to media sources, two days before the deadline expired Vornado sought to renegotiate key terms of the lease. The *New York Times* reported that Vornado insisted on a 39-year lease instead of the required 99-year lease, and refused to “put up \$100 million in a show of good faith as the contract was signed but before the deal closed.” The PA viewed Vornado’s renegotiation efforts as a “last minute attempt to wring a concession” over nonnegotiable items, and on March 19, 2001 awarded the lease to Silverstein Properties Inc. One top executive at the PA said: “Vornado is very difficult to deal with. I think the time factor was insurmountable.” Mary Ann Tighe, a well-known New York City real estate executive, said: “It’s both a surprise and yet completely predictable given Vornado’s historic negotiating approach. These guys know how to win a bid, but they also know how to attempt to restructure the deal to make it more favorable.”

When the consultants asked Steve Roth about his failed dealings with the PA in 2001, he stated that this was the “largest real estate deal in the history of man,” and that Vornado was awarded the deal and agreed to complete it in 21 days. Mr. Roth said that he assumed that because of the complexity of the transaction (including engineering

problems), the PA would never insist on closing in just three weeks. What happened next, according to Mr. Roth, was that “[o]n the 16th day, my guys said ‘these guys are serious.’” When Mr. Roth objected to the deadline, the PA awarded the lease to the second lowest bidder.

A comprehensive media review, consisting of over 30,000 print and Internet sources, identified numerous references to Wynn Resorts and/or its subsidiaries or Stephen Wynn, personally, but only a few are of particular interest. For example, an article published in the *Times Union* (Albany, NY) in 2006, indicated that Wynn Resorts’ current general counsel, Kim Sinatra, “got in trouble with the [New York] state lobbying commission when Assembly Speaker Sheldon Silver received perks and discounts at a Las Vegas casino/hotel,” when she worked at Caesar’s Entertainment. In relation to the same incident, a March 16, 2004, *New York Times* article said that Assemblyman Silver received “steep discounts” when he stayed at the Paris Las Vegas in 2002 and dined with his wife at the hotel with “one of the company’s lobbyists, Kim Sinatra.” Sinatra left Caesar’s in January 2003 and did not join the Wynn organization until January 2004. During an interview, Ms. Sinatra acknowledged her role in the Caesar’s events, but Sinatra pointed out that this occurred before she joined Wynn.

In the consultants’ May 3, 2007 interview of Stephen Wynn, he disclosed that there are three junket representatives operating at Wynn Macau, and all are licensed as such by the Macau government. One of these companies, called International, is run by an individual named Jack Lam. A 2006 Chinese-language tabloid called *Next Magazine* reported that Lam Changxing, “China’s most wanted fugitive,” was a major junket operator in Macau, operating one VIP room in Wynn Macau and one VIP room in

Stanley Ho's Grand Lisboa. An April 2, 2007 *Las Vegas Sun* article described Ho as a "Macau casino boss with reputed links to Chinese organized crime." A 2006 *Las Vegas Business Press* article quoted an industry observer who said, "It has long been believed by those on the ground [in Macau] that Ho's casinos were infiltrated with triad gangs with ties to the VIP-room subcontractors and junket operators." Additionally, with respect to Jack Lam and Stanley Ho, a March 21, 2006 *Manila Standard* article quoted a Filipino senator, Jinggoy Estrada, calling Lam "an alleged associate of a certain Stanley Ho, the reported kingpin of the gambling empire in Macau."

During the consultants' interview of Mr. Wynn, he was shown a May 1, 2007 *Star-Ledger* article that said the New Jersey Division of Gaming Enforcement had conducted an investigation for the past year and a half into MGM Mirage's partnership in Macau with Stanley Ho's daughter, Pansy Ho. According to the article, "for decades, Stanley Ho has been dogged by allegations that he has ties to the Chinese mob." MGM was able to enter the Macau market by partnering with Pansy Ho and paying Stanley Ho a \$200 million sub-concession, the article said. The article speculated that in a worst-case scenario, the New Jersey regulator could decide that Pansy Ho is too close to her father for her to be an appropriate partner for a New Jersey license holder. Mr. Wynn responded by saying that he has gone to see Stanley Ho on three occasions to pay his respects. Wynn further pointed out that there is no evidence that Ho is a criminal. With respect to Jack Lam, Kim Sinatra (Wynn Resorts' general counsel who was also present during the interview of Mr. Wynn) said that Wynn Resorts is aware of concerns about Lam and is keeping a close eye on the issue. To illustrate how serious he is about

compliance, Mr. Wynn stated that he has hired the head of the organized crime unit of the Hong Kong police department.

Aruze Corporation in Japan is the sole owner of Aruze USA Inc., which in turn has a 24.33 percent interest in Wynn Resorts Limited. Japanese businessman Kazuo Okada controls Aruze Corporation. A 2000 *Reuters News* article reported that Okada announced he was investing \$260 million in Valvino Lamore, becoming a 50 percent owner of the current subsidiary of Wynn Resorts. The following month, the Tokyo Regional Taxation Bureau announced that it had ended its criminal investigation into Aruze, charging it with hiding \$35 million in income from 1996 to 1998 through software development expenditures made by an Aruze subsidiary to Universal Distributing of Nevada, according to a 2000 Japanese-Language *Nikkei Shimbun* article. Aruze was originally fined \$14.9 million, but the Tokyo District Court overturned the fine in 2002, according to a 2002 *Las Vegas Sun* article. After the company was originally fined in December 2000, the Nevada Gaming Control Board voted to send Aruze's license application back to staff for further investigation rather than approve the acquisition, according to a 2000 *Las Vegas Review-Journal* article.

Mr. Wynn's personal counsel, Frank A. Schreck, was also present during the interview of Mr. Wynn. Schreck stated that he is particularly familiar with the allegations involving Okada and Aruze because, in addition to representing Mr. Wynn, Schreck is the head of Aruze's compliance committee. Schreck told us that the tax and related allegations were generated by a particular Nevada Gaming Board investigator who misunderstood the facts of the matter. Schreck said that the tax matter was resolved

when the Tokyo court overturned the fine, and the Nevada gaming aspect was resolved when Okada was licensed by the gaming board.

Stephen Wynn was the subject of a book published in 1995, entitled *Running Scared: The Life and Treacherous Times of Las Vegas Casino King Steve Wynn*. The *New York Post* reported on May 2, 2007, that the book “has mysteriously appeared in the offices of state lawmakers.” Although the book raised allegations of organized crime involving Mr. Wynn, it should be emphasized that Mr. Wynn has since been licensed by gaming authorities in Nevada and Macau. In response to the media attention this book garnered in 1995, Mr. Wynn produced 16 affidavits from former FBI and other law enforcement officials saying that they had never found evidence of his having an improper relationship with organized crime figures. Furthermore, Mr. Wynn sued the publisher of the book for libel and won a \$3.1 million verdict, though the verdict was later overturned. The lawsuit was settled in 2004 for an undisclosed amount, according to a media article, and the publisher issued an apology saying that he had never intended to “state or imply that I believed you [Steve Wynn] were the front man for the Genovese family.”

Numerous articles were identified on-line for Gerald “Jerry” Bilinski, regarding his relationship with New York State Senate Majority Leader Joseph Bruno and his resignation as chairman of the New York State Racing and Wagering Board due to ethics violations. According to a December 2006 *The New York Times* article, Jerry Bilinski, reportedly a close friend and co-owner of horses with Senator Bruno, was a recipient of a federal grand jury subpoena issued in an ongoing FBI probe of Senator Bruno. Furthermore, the article mentions that in November 1996, “after receiving two

anonymous tips,” the State Inspector General reportedly found that Bilinski “improperly used state money” for trips to Fort Lauderdale, Florida and to Louisville, Kentucky, the details of which are discussed in detail above.

Media reports also described a 1996 New York State Ethics Commission investigation into whether Bilinski, as Chairman of the New York State Racing and Wagering Board, “violated the Public Officers Law with respect to activities in which he engaged related to the ownership and breeding of thoroughbred racehorses.” A Notice of Reasonable Cause was issued, alleging that Bilinski, on 14 occasions, violated ethics laws by selling breeding rights to licensees of the Board, and, on 16 occasions, violated ethics laws by creating and maintaining partnerships to own horses with a licensee of the Racing and Wagering Board. Bilinski reportedly resigned as chairman of the Racing and Wagering Board after “refusing to comply with a State Ethics Commission order to divest his horse ownership interests.” Those interests, the Ethics Commission said, conflicted with his stewardship.

In his interview, Bilinski stated that in 1995, Senator Joseph Bruno, a friend and veterinary client, asked Bilinski to become Chairman of the Racing and Wagering Board, and he accepted. He stated that the Ethics Commission found him guilty of two violations while he was Chairman of the Board. One violation related to a result of a breeding and boarding operation Bilinski operated, Waldorf Farms, at the same time he was the Racing and Wagering Board Chairman. In December 1995, a former Waldorf Farm employee, then working at the Racing and Wagering Board, gave his Racing and Wagering phone number to a person at *Blood Horse Magazine*. The phone number appeared as the contact number for a Waldorf Farms advertisement in the magazine. The

Ethics Commission investigated and told Bilinski he had to divest himself of his breeding operation or resign from the Board. He said that he resigned because he could not afford to divest. He said he informed the state of his business dealings in his application, and felt any conflicts should have been noticed then.

Media reports cited that The Friends of New York Racing, a “short-termed advocacy group formed by racing fans and executives intent on overhauling the Aqueduct, Belmont and Saratoga tracks,” and one of its founding directors, Jared Abbruzzese (who prior to his resignation in October 2006 was a member of Empire Racing’s board), came under investigation by the New York Temporary State Commission on Lobbying and a federal grand jury in 2006. The Lobbying Commission reportedly is looking into whether Abbruzzese violated state law by giving free or discounted flights to Senator Joseph Bruno, and the federal grand jury is looking into whether substantial payments made by Abbruzzese to “Bruno’s private consulting firm were part of an effort to influence the senator.” According to media reports, R. Wayne Diesel was on the board of Friends at the time of these alleged violations. According to a *New York Times* article dated March 26, 2007, the investigation is ongoing.

Media articles, written between 1988 and 2003, detail four separate suspensions of Gary Contessa, resulting from positive drugs tests of his horses. In his interview, Contessa explained the four instances when drugs were found in horses he trained. In the first instance, officials found ephedrine in one of Gary Contessa’s feed products and eight of his horses tested positive for this drug. The second instance involved caffeine. Contessa explained that he trains a horse for Ted Banker of the New York Jets football team. Before a race, Banker visited the horse with Joe Klecko, a former Jet, and they

thought it would be fun to feed the horse a PowerBar. Banker testified to this and paid Gary Contessa's fine. The third instance involved one of Contessa's horses, which was administered the drug lidocaine following a surgical procedure. A horse would normally be held from racing for 14 days afterward, because the drug metabolizes in the system slowly. The operation was delayed one week and the horse was still on lidocaine when they tried to race it, and it tested positive for the drug. The fourth instance, involving ambroxyl, occurred because Contessa's horses had trouble breathing when they raced at the Meadowlands, so Dr. Robert Fritz created a nebulizer solution to aid the horses in breathing when they raced. Ambroxyl is not FDA approved. The horses tested positive for the drug, and it was traced back to Dr. Fritz.

According to media reports, Philip Parenti, formerly the administrator of the Illinois Gaming Board, has been criticized for accepting an executive position at Harrah's Entertainment while he was still with the Gaming Board. At the time, the Gaming Board's code of ethics barred a board employee from taking a job with an Illinois casino operator for a year after he leaves state employment. Parenti did not technically violate this rule, as Harrah's was a parent company of an Illinois casino operator, and not directly operating a casino in the state. However, after Parenti's departure, the code was amended to prohibit employment with a parent company or subsidiary of a company operating a casino within the state for two years after leaving the board. In another instance, media reports indicate that Parenti came under criticism for his negotiations with the bankrupt Emerald Casino when the casino was trying to sell its license. According to the reports, Parenti proposed a settlement in the potential sale that would benefit the investors of the casino more than the State of Illinois. Parenti maintains that he acted on behalf of the state in his negotiations..

CAPITAL PLAY, INC.

Capital Play, Inc., is one of the four entities seeking the award of the franchise to conduct racing and pari-mutuel betting at New York's three major thoroughbred racetracks. Capital Play, Ltd. was incorporated in the State of New York on March 14, 2007 to serve as a temporary vehicle for securing financing and participating in the franchise bidding process. Capital Play Ltd. will be merged into Capital Play, Inc., the permanent entity, if it is awarded the franchise. The only shareholder in Capital Play Ltd., the temporary entity, is Karl O'Farrell. Capital Play Ltd. conducts no operations and has no active officers, directors, or additional shareholders. As discussed below, Mr. O'Farrell was also a majority owner of Capital Sports, Ltd., located in Australia, which was one of ten simulcast companies whose contract authorization was withdrawn by the Racing and Wagering Board after NYRA terminated its contract.

Key Persons and Business Entities

A number of changes to the structure of Capital Play have occurred during the course of the integrity review process. The identities of debt and equity providers and their respective commitments to Capital Play have changed, with references having been made to discussions having taken place with a number of individuals and entities, including Connecticut's Foxwoods Resort and Casino to serve as gaming partners or investors. In addition, an agreement with Scotia Capital was signed on April 11, 2007 to provide advisory services and to identify an equity provider to finance Capital Play Ltd.'s bid for the franchise. Not until May 1, 2007, however, were the debt and equity providers below identified.

- Debt Financing - On March 30, 2007, CIBC World Markets issued a highly confident letter indicating that it commits to provide \$550 million of debt financing contingent on a variety of factors, including Capital Play Ltd.'s securing a substantial amount of equity investments. Based on discussions with a representative of CIBC, it appears that CIBC will ultimately syndicate its debt commitment to Capital Play Ltd. to other investors, who at present are unknown or not identified.
- Equity Investment - On April 20, 2007, Plainfield Asset Management (Plainfield) executed a term sheet to provide up to \$250 million in equity financing, contingent on certain factors, including Capital Play Ltd.'s being awarded the franchise. According to representatives of Capital Play Ltd., Plainfield may ultimately syndicate its position in Capital Play Ltd. to other investors who, at present, are unknown or unidentified. Plainfield will assume a seat on Capital Play's board and may also play a key role in the management of the entity.

Mr. O'Farrell's own financial commitment to Capital Play has not been finalized. He indicated that his personal investment in the venture is in the range of \$5 million to \$7 million. According to Mr. O'Farrell and his accountant, this commitment was made through two Australian entities in which Mr. O'Farrell has an ownership interest and reflects a repayment of prior loans that he had personally made to these entities.

Prior to May 9, 2007, 11 individuals from Australia and the U.S. had been identified as key persons by Capital Play Ltd. They are, in addition to Mr. O'Farrell, James Colquhoun, Paul Brettell, Mark Owens, Jeffrey House, Tony Charara, Jon Ellwood, David Nolan, Andrew Goodell, John Schreck, and John Pavia. It is

contemplated by Mr. O'Farrell that each of these persons may ultimately have a key management role and/or an equity interest in the operation. Each of these individuals submitted a Key Person Integrity Questionnaire (KPIQ). Mr. O'Farrell will be the company's President and Chief Executive Officer. James Colquhoun will serve as Chairman. Determination of the operational structure and identity of additional members of Capital Play's management team are, as in the case of the other bidders except NYRA, pending the award of the franchise.

In addition, various individuals and entities were identified as being advisors to Capital Play Ltd. Andrew Goodell was identified as its legal advisor. The remaining individuals, whose names follow, were those whose services were retained in connection with the bidding process: Morton Finder; Andrew Ro; Joe Logan; Michael Weitz; Blue Chip Farms; Richard S. Mezan, P.C.; Ronald Goldstock; Andrew Frank; Hank Sheinkopf; Fred Polsinelli; Dick Stern; Eight Inc. and Todd Ehrlich. According to Capital Play, Mr. Goldstock will undertake certain Independent Private Sector Inspector General services with respect to Capital Play Ltd's business practices. The services will include monitoring the implementation of, and adherence to, the company's internal controls and code of ethics.

Along with Capital Play's initial consultant engagement letter, on or about April 19, 2007, Mr. O'Farrell signed a second engagement letter to obtain the required consultant services with respect to Capital Play's significant new business entity, Plainfield Asset Management, LLC. Moreover, it was not until May 4, 2007 that the consultant received the first of five submitted questionnaires relating to Plainfield. Given the shortened time period within which to conduct the review of Plainfield, the consultant's research was, by necessity, more limited.

On May 26, 2007, Capital Play issued a press release announcing that the real estate development firm Related Companies, led by Chairman and CEO Stephen Ross,

had joined Capital Play in its effort to secure the racing franchise. In view of the timing of this addition, this report does not include an analysis of either Mr. Ross or Related Companies. This analysis will begin shortly and the results will be submitted to the Committee as an addendum to this report.

Plainfield Asset Management, LLC

According to the Delaware Division of Corporation records, Plainfield Asset Management, Capital Play's major equity partner, filed as a limited liability corporation (LLC) on February 14, 2005. According to its Business Entity Integrity Questionnaire (BEIQ), Plainfield is an investment advisor to, among others, Oneida Entertainment II, LLC (Oneida) and Plainfield Special Situations Master Fund Limited (Plainfield Master Fund.) BEIQs were submitted by Plainfield Asset Management, Plainfield Master Fund and Oneida. According to the BEIQ submitted by Plainfield Asset Management, its key persons are Achim Maximilian Holmes, Joseph C. Bencivenga, Niv Harizman, Georges Holzberger, Terri Lecamp and Robert D. Sherman. According to the BEIQ submitted by Plainfield Master Fund, its key persons are Achim Maximilian Holmes, David Bree and Aldo Ghisletta. In its BEIQ, Oneida stated that its key persons are Achim Maximilian Holmes and Joseph C. Bencivenga. KPIQs have been submitted by Achim Maximilian Holmes and Joseph C. Bencivenga.

According to its BEIQ, Plainfield is indirectly related to the following entities that are engaged in racing or gaming: American Gaming Group, LLC; American Racing and Entertainment, LLC; Wyoming Entertainment, LLC; Edgewater Casino; Snolqualmie Entertainment Authority; and Riviera Holdings, Inc. Its relationship to each entity is as follows:

- American Gaming Group, LLC – Plainfield Gaming III, Inc. has a 20 percent interest in this entity, which has submitted a gaming license application for a proposed casino in Colorado. Plainfield Gaming III, Inc. is an indirect subsidiary of Plainfield Master Fund.
- American Racing and Entertainment, LLC – Oneida Entertainment, LLC owns 44.59 percent of this entity, which operates the Tioga Downs and Vernon Downs racetracks in New York. Oneida Entertainment, LLC is an indirect subsidiary of Plainfield Master Fund. According to Oneida’s BEIQ, American Racing and Entertainment, LLC holds a Video Lottery and Racing License from the New York State Racing and Wagering Board.
- Wyoming Entertainment, LLC – Plainfield Racing, Inc. has an 80 percent interest in this racing and off-track betting venture. Plainfield Racing, Inc. is an indirect subsidiary of Plainfield Master Fund. According to Oneida’s BEIQ, Wyoming Entertainment, LLC holds a Racing and Simulcasting License from the Wyoming Pari-Mutual Commission.
- Edgewater Casino – Plainfield Gaming, ULC indirectly holds an interest in Edgewater Casino, a registered casino operator in British Columbia. Plainfield Gaming, ULC is an indirect subsidiary of Plainfield Master Fund.
- Snolqualmie Entertainment Authority – Plainfield Gaming II, LLC owns debt issued by Snolqualmie. Plainfield Gaming II, LLC is a subsidiary of Plainfield Master Fund.
- Riviera Holdings, Inc. – Plainfield Master Fund owns 8.84 percent of common stock in Riviera Holdings, Inc., a gaming management and casino operator.

Affiliations with Rebate Shops

Capital Play Pty Ltd. (Australia) is a wholly-owned subsidiary of Karrell Pty Ltd., an entity whose majority owner is Karl O'Farrell. Mr. O'Farrell acquired his holdings in Capital Play Pty Ltd. as part of the settlement of a legal dispute against Canbet Limited. Capital Play Pty is a Canberra-based bookmaking operator which is licensed by the Australian Capital Territory Gaming and Racing Commission (ACTGRC) and provides wagering services to Australian residents who bet on horse races in North America. Currently, it has agreements with 55 racetracks in North America. Since its inception, Capital Play Pty Ltd. (and its predecessor Capital Sports Pty Limited) has employed a maximum 25 people, and currently has two full-time and two to four part-time employees and advisors.

Since 2003, Capital Play Pty Ltd. has provided services to two primary clients or "syndicates" (designated as CAP01 and CAP02), together comprising 28 individuals. Historically, the two syndicates together have wagered approximately \$200 million (AUS) per year with Capital Play Pty Ltd. The screening of individual bettors, in particular with respect to the nature of their businesses, backgrounds, and sources of funds, is limited.

Capital Play Pty Ltd. offers loyalty payments, or rebates, to its customers based on the volume of bets placed. These rebate payments are determined by Capital Play Pty management on a monthly basis and generally reflect 10 to 12 percent of the totals

wagered.¹⁸ According to the ACTGRC, it is satisfied that Capital Play Pty Ltd. has not violated any ACTGRC rules by engaging in rebate betting. In general, Capital Play's policies and procedures have been assessed by the ACTGRC on a periodic basis and have been found to be satisfactory.

Mr. O'Farrell stated in his key person interview that Capital Play Pty Ltd.'s policy is to avoid cash payments by bettors and that he was comfortable with the source of funds from the two syndicates. He stated that each syndicate made an initial deposit with Capital Play Pty Ltd., in the amounts of \$60,000 (AUS) and \$200,000 (AUS), respectively, and that no subsequent deposits were made. Each was so successful that all subsequent betting by the two entities over the period 2003 to 2007 was financed from winnings and customer loyalty payments made by Capital Play Pty Ltd.

Based on available financial information, Capital Play Pty Ltd.'s net losses have totaled approximately \$2.8 million (AUS) for the four fiscal years ending June 2001 to June 2004. In 2005, Capital Play Pty Ltd. recorded net income of approximately \$596,000 (AUS) and in 2006, net losses were approximately \$404,000 (AUS). Mr. O'Farrell stated that for the year ending June 30, 2007, it is expected that revenues will decrease by 50 percent to approximately \$17.5 million (AUS) and that the company will "break even" from a net profit perspective. According to Mr. O'Farrell, the drop in revenues is due to the entire loss of business from one of its two syndicate customers and the decrease in volume of business from the other syndicate customer. Mr. O'Farrell

¹⁸ Customer statements, documentation regarding calculations of loyalty awards and other documentation were not furnished as of the preparation of this report.

stated that based on this drop in revenue, he is considering alternate business strategies for the company, including focusing on Internet-based retail players and expanding to other international markets. According to the ACTGRC, no bets have been placed with Capital Play Pty Ltd. since December 5, 2006.

Capital Play is the only licensed bookmaker in the ACTGRC to accept bets in North America. In his integrity questionnaire, Mr. O'Farrell stated that Capital Play Pty Ltd.'s most significant assets are the license from the ACTGRC, valued between \$10 million (AUS) and \$20 million (AUS), and its agreements with horse racing tracks in North America. In addition to these described business activities in Australia and the U.S., Capital Play Pty Ltd. has pending simulcast applications with the United Kingdom, France, and South Africa, and has been negotiating for a gaming and racing license in Macau. Mr. O'Farrell stated that if selected to operate the New York State franchise, Capital Play Pty Ltd. will continue to operate in Australia, but that he would likely limit his involvement with the Australian entity and focus his attention on the United States.

Capital Play Pty Ltd.'s operations are dependent on simulcast signals to transmit information to and from horse racing tracks. Its simulcast signal from the three New York State thoroughbred horse racing tracks had been provided by NYRA with the approval of the New York State Racing and Wagering Board. In January 2005, NYRA notified Capital Play Pty Ltd (then called Capital Sports Pty Ltd.) that it was terminating its simulcast contract effective January 31, 2005. The simulcast signal to Capital Play Pty Ltd. has not been reinstated.

As discussed previously, in January 2005, NYRA announced that it was terminating its simulcast agreements with the four operating rebate shops named in the *Uvari* Indictment prosecuted by the U.S. Attorney's Office for the Southern District of New York. The indictment alleged instances of illegal gambling, money laundering, and horse doping. Capital Sports Pty Ltd. was not one of these four entities. However, NYRA subsequently notified six additional simulcast licensees, including Capital Sports Pty Ltd., that it was terminating their simulcast contracts. On January 27, 2005, Racing and Wagering issued a letter to all of New York's racetrack presidents and general managers, in which it withdrew its approval for any contracts between New York simulcast licensees and ten specified entities, including Capital Sports Pty Ltd. In a letter to NYRA dated February 18, 2005, James Colquhoun, Chairman of Capital Play Pty Ltd. stated that NYRA had "unilaterally and without cause" cancelled Capital Sports' contract and sought immediate reinstatement of the contract. To date, reinstatement has not occurred. Subsequent to the NYRA termination, Capital Sports Pty Ltd.'s signal from the Keeneland Race Course in Kentucky was cut off by the track operator.

During its appearance at the public hearings held on April 11, 2007 in Albany, New York, members of the panel noted that NYRA, during its presentation, apparently stated that it canceled the simulcast agreement with the Australian entity Capital Play Pty Ltd. due to an industry practice known as "batch betting." According to the panel, NYRA described the term batch betting as, "using technology as a means to find information and make bets at the last minute" before a race starts. In response, Capital

Play representatives stated that this was the first time that they were made aware of such an explanation for the simulcast cut-off. It should be noted that batch betting is not illegal in New York or other states.

During the course of this integrity review, an interview was conducted with Robert Feuerstein, General Counsel for Racing and Wagering, regarding the simulcast cut-off of Capital Play Pty Ltd. Mr. Feuerstein stated that rebates, while not per se unlawful, were prohibited as a matter of policy by Racing and Wagering until 2006. The decision by Racing and Wagering to withdraw approval of simulcast contracts, including that of Capital Play Pty Ltd., was based on NYRA's cut-off, and that the allegations of being a rebate shop violated the terms of the simulcast agreements. He acknowledged that Racing and Wagering did not perform any due diligence or investigation with respect to Capital Play Pty Ltd. in connection with the simulcast cut-off, and that his office, the Office of General Counsel, was not involved in issuing Racing and Wagering's January 27, 2005 letter withdrawing its approval. Moreover, two of the ten rebate shops that had been subject to simulcast termination subsequently were reinstated by NYRA. Acknowledging that Racing and Wagering has no specific policy prohibiting batch betting, he stated that it is currently reviewing the practice, adding that it is primarily concerned that bets are not placed on a race after the official close.

Mr. O'Farrell stated that as part of its efforts to have its simulcast signal reinstated and its reputation restored, Capital Sports Pty Ltd. submitted an application in July 2005 through the New Jersey Sports and Exposition Authority requesting that the Thoroughbred Racing Protective Bureau (TRPB) perform a due diligence investigation of Capital Sports Pty Ltd. The TRPB performed a review of Capital Play Pty Ltd. and

issued “a clean bill of health,” according to Mr. O’Farrell. The TRPB report was issued in 2006 and was shared with various state regulators and horse racing tracks with which Capital Play Pty Ltd. has simulcast arrangements. Mr. O’Farrell stated that Capital Play Pty Ltd.’s attempts to have the simulcast signal reinstated consisted of numerous attempts to speak with NYRA representatives, but that “his calls were not returned.” He asserted that the termination of the simulcast signal by NYRA was without merit, was a poor business decision, and that, in his view, the termination was driven by NYRA’s attempt to remediate its own serious integrity problems at the time.

Discrepancies and Omissions in Responses to Questionnaires

Certain individuals submitted their Key Person Integrity Questionnaires without the requisite notarizations. Not until the last few days, prior to the writing of this report, did Karl O’Farrell provide his tax returns which are currently being reviewed. Achim Maximilian Holmes of Plainfield failed to respond to the question in the KPIQ asking if Holmes “had been advised of being the target or subject of an investigation involving any violation of criminal law.”

Legal and Regulatory Issues

Tony Charara disclosed that in or about 2005 he had been convicted in Australia of an offense relating to his failure to file tax returns for the years 2000-2002. He stated that he had no tax deficiency for this period and was fined \$1,000.

James Colquhoun was involved in a lawsuit related to the lease of a racehorse in which he owned an interest.

Mr. O'Farrell is a defendant in a recent lawsuit that was brought by Palicave Pty Ltd. (Palicave). Two of the individual betters associated with Capital Play Pty Ltd.'s CAP01 syndicate were John Wilson (a/k/a Zeljko Ranogajec) and Shelly Wilson (wife of Mr. Ranogajec). Both are also the main principals in Mountain Lake and Palicave. These individuals are well known in the wagering industry in Australia. This contractual dispute revolves around the conversion of debt to equity of approximately \$2 million (AUS) with respect to a loan agreement made to Mr. O'Farrell. According to Mr. O'Farrell, Palicave made two loans to him. The first loan was made in June 2002 for a total of \$1.25 million (AUS) to fund start-up costs of Capital Sports Pty Ltd. The second loan was extended in August 2004 and was used by Mr. O'Farrell to buy out Mountain Lake's equity position in Capital Sports Pty Ltd. In May 2006, Mr. O'Farrell and Palicave attempted to convert Palicave's debt position to an equity interest in Capital Sports. Mr. O'Farrell's request for an informal approval of the transaction from the ACTGRC was denied due to Mr. and Mrs. Wilson's ownership in Palicave and their non-compliance with an earlier probity request for Mountain Lake. (The ACTGRC had disallowed a planned transaction to transfer the majority holdings of Capital Play Pty Ltd. to Mountain Lake.)

The ACTGRC is currently investigating a recent complaint by the CAP01 syndicate regarding the payment of a rebate totaling \$8 million (AUS). ACTGRC views the dispute between Capital Play Pty Ltd. and the syndicate as reflecting a business dispute rather than a betting issue. Mr. and Mrs. Wilson are also major shareholders in the CAP01 syndicate that, according to Mr. O'Farrell, has stopped placing bets with Capital Play Pty Ltd. It also appears that Mr. Wilson was also a major shareholder in the

CEL group of companies, an entity that Mr. O'Farrell was previously associated with. According to media articles, "Mr. Wilson, A/K/A Zeljko Ranogajec, is Australia's, and possibly the world's biggest [bettor], and strikes fear into the heart of every bookie. Mr. Wilson boasts gambling turnover of about \$1 billion a year. An estimated \$200 million is bet in Australia. He has agents betting for him with bookmakers, but he basically controls the totes. His talent for counting cards soon had him banned from casinos including Wrest Point in Tasmania". ACTGRC reports that they are aware of these individuals and their reputations, and of their business ties to Mr. O'Farrell. The ACTGRC does not take issue with them being Capital Play's individual bettors.

Mr. O'Farrell disclosed in his questionnaire that in the past he had business relationships with various members of the Waterhouse family which have since been severed. Apparently, the Waterhouse family is synonymous with Australian racing and betting. Robert Waterhouse and his father Bill are described by Australian media as owning a chain of betting shops in Fiji and in Vanuatu. Robert Waterhouse is a bookmaker who was banned for life from the racing industry in Australia as a result of a 1984 scandal involving horse doping and/or switching and betting using insider information. His ban was lifted in 1998.

Mr. O'Farrell's business relationship with the Waterhouse family included a shared ownership in Network Entertainment Group Ltd. from 1997 through 1999, and a number of advisory roles in business ventures that did not materialize. Australian media reports describe Mr. O'Farrell as a former close friend and business associate who was "bailed out" by the Waterhouse family. Mr. O'Farrell confirmed a 1999 transaction which consisted of a cash infusion to his video distribution business, Network

Entertainment. This transaction resulted in 30 percent ownership in the company to the Waterhouse family. According to Mr. O'Farrell, after acquiring Capital Sports in 2002, he submitted a letter to the ACTGRC stating that he would have no business dealings with any of the Waterhouse family. He stated that he has not been in contact with Robert Waterhouse since 2002 and that at no time was he an employee or acted in a management capacity of any Waterhouse family businesses.

Judgments, Liens, and Bankruptcies

Searches for judgments and liens did not reveal any filings for the individual key persons.

Political Contributions and Lobbying

Searches for political contributions or lobbying contracts did not reveal anything of significance.

Media Reports

The following news stories relate to Capital Play and/or its affiliates.

A March 20, 2007 article in *The Herald News* (Passaic County, New Jersey) reported that the New Jersey Department of Environmental Protection and the Meadowlands Commission sued Plainfield Asset Management in regard to a railway transfer station in North Bergen County, New Jersey. Plainfield was sued, according to state officials, because it has "invested heavily" in the station. According to state officials, 1,500 tons of debris that would be handled each day at the site could harm nearby residents because "some of the waste could be toxic." The lawsuit said that "the dust generated by all the debris would not meet state standards" and asked the court to

halt construction until the station complies with all state regulations. A Plainfield spokeswoman would not comment on either the lawsuit or the company's investment.

An April 26, 2007 article in *Observer-Dispatch* (Utica, New York) reported that Houston-based Nevada Gold and Casinos, Inc. "was pulling out" of Vernon Downs and Tioga Downs racetracks in New York, both operated by Plainfield's affiliate. Nevada Gold and Casinos, Inc. was in the process of selling its 23 percent stake in American Racing and Entertainment, which owns both the racetracks, to its partners Southern Tier Acquisition II, LLC and Oneida Entertainment, LLC. Oneida Entertainment and another partner, New York City businessman Jeff Gural, will reportedly invest \$4.3 million in the purchase. Nevada Gold and Casinos, Inc.'s CEO stated that the company was unlikely to invest in another racing facility in New York unless there were major changes to the tax rates. Racetracks in New York State reportedly pay 60 percent of their revenue to the New York Lottery, which greatly affected Vernon Downs. Vernon Downs' closest competitor is Turning Stone Resort and Casino, an Oneida Indian Nation-owned entity that is not taxed. An April 24, 2007 article in *The Post-Standard* (Syracuse, New York) reported that a longtime stockholder in the Vernon Downs stated, "...this is a warning sign that all isn't going well."

A March 23, 2007 article in *The Post-Standard* (Syracuse, New York) reported that in order for Vernon Downs to be able to race in April, the racetrack had to satisfy more than \$6 million in loans to a former investor and a Las Vegas mortgage company. Jeff Gural stated that if the tax law did not change, Vernon Downs would probably close since, "it doesn't make sense to keep losing money." According to Gural, Vernon Downs loses about \$500,000 a month, with revenues averaging about \$575,000 per week, much

less than that \$1 million a week needed to realize a profit. Vernon Downs owes Vestin Mortgage Company of Las Vegas a total of \$22.8 million, of which \$3 million was due March 31, 2007. Gural stated that he and Oneida Entertainment planned to satisfy the loans. A December 28, 2005 article in *The Post-Standard* reported that Oneida Entertainment was a partnership between Plainfield Asset Management and San Diego businessman Eric Spector.

A January 25, 2006 article in *The Post-Standard* reported that Oneida Entertainment agreed to withdraw its plan to bring Vernon Downs out of bankruptcy and to withdraw its objections to the plan submitted by Vernon Downs Acquisition. In exchange for the withdrawals, Oneida Entertainment would become an investor in Vernon Downs Acquisition. A January 7, 2006 article in *The Post-Standard* reported that a lawyer in the bankruptcy “hinted in court” that the Oneida Indian Nation might be behind Oneida Entertainment. The lawyer, who represented two Vernon Downs stockholders, said lawyers in the case have been trying to determine “whether or not an Indian nation is involved” in the company. A lawyer for Oneida Entertainment “heatedly denied in court” that the Oneida nation is involved. A December 29, 2005 article in *The Post-Standard* reported that the Oneida Entertainment plan “didn’t win support from any of several classes of creditors.”

CONCLUSION

The information set out in the report is the product of an extensive due diligence review of literally thousands of documents, augmented by individual interviews of key persons, industry experts, witnesses having relevant information to offer, as well as contacts with law enforcement and regulatory officials in New York State, in other states, and in foreign countries. All of the relevant information available bearing upon the integrity of each of the entities seeking the franchise, as well as their equity owners and key personnel, has been carefully scrutinized. All significant negative information relating to the integrity of a potential franchisee is reflected in this report.

While key investors and management personnel continued, in many cases, to change throughout this process, such changes continue even as this report is submitted to the Governor's Selection Committee. Where such future changes are deemed to be structurally significant or bear directly upon the integrity of the franchise candidates, additional analyses will be performed, and addenda to this report, where appropriate, will be submitted to the Committee.

As the Committee has sought to apply the highest standard of integrity and ethics, and has made such considerations the very hallmark of the process, we trust that this report makes an important contribution in this regard.