



The Kentucky Thoroughbred Breeding Industry And State Programs That Assist The Equine Industry

Research Report No. 406

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Abstract

Nationally, the number of Thoroughbred mares bred decreased over the past two decades. Thoroughbred breeding in Kentucky grew for most of this time period but has decreased in recent years. In spite of the recent declines, Kentucky has gained market share and remains the dominant state in the Thoroughbred breeding industry. In 2010, Kentucky accounted for 43 percent of the Thoroughbred mares bred in the US. Kentucky assists the horse industry by allocating the sales tax from stud fees to fund awards to breeders based on their foals' performances in races, shows, or contests. The state also allocates a portion of pari-mutuel tax revenue to supplement horse racing purses. Recent declines in Thoroughbred breeding and pari-mutuel wagering have led to less funding for these assistance programs. In 2010, Kentucky's Thoroughbred breeding industry created an estimated 17,600 Kentucky jobs within the industry and in other sectors that provide goods and services to the industry. The total earnings for all jobs created were estimated to be more than \$350 million.

Foreword

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Summary

The Program Review and Investigations Committee directed staff to examine Kentucky's Thoroughbred farms, identify trends related to the Thoroughbred breeding sector, examine programs designed to assist the industry, and estimate the economic contribution that Thoroughbred breeding farms make to the state. The report has one recommendation.

Survey Of Kentucky Thoroughbred Farms

Owners and managers of 150 Kentucky Thoroughbred farms responded to a survey done as part of this study. The results of the survey indicated a small percentage of the farms accounted for most of the horses, income earned, and spending by Thoroughbred farms in Kentucky.

For most of the respondents, the primary focus of their operations related to the broodmares they owned and the sales of the offspring produced. Twenty-five percent of the respondents indicated their operation was diversified, and that in addition to having broodmares of their own, the farm offered a range of services such as boarding, training, sales preparation, and stud services. Twenty percent of the farms boarded horses for others and depended on boarding fees for most of their income.

Based on the survey results, the average Thoroughbred farm in Kentucky is 369 acres with 59 horses. Most of the horses on the Thoroughbred farms surveyed were owned by the farm, but 40 percent were owned by others and boarded at the farm. Two-thirds of the farms had fewer than 50 horses each, accounting for 24 percent of the total horses. One-third of the farms each had more than 50 horses; these farms accounted for 76 percent of the total horses.

A majority of the farms indicated they had full-time and part-time employees. Seventy-eight percent of the employees were full time, and 22 percent were part time. More than 60 percent of the farms had 5 or fewer employees. The average number of full-time employees on the farms that responded to the survey was 13; the average number of part-time employees was 4.

Farms that responded to the survey earned income from stud fees, from weanling and yearling sales, and by providing boarding services to clients. Other income earned by these farms came from sales preparation fees and commissions. Most of the income generated by the Thoroughbred farms that responded to the survey was concentrated among a relatively small percentage of the farms.

History

Prior to the early 20th century, Kentucky's position in the Thoroughbred industry varied significantly. Sometimes, Kentucky was the leader or among the leaders in the industry; at times other states or regions were dominant. A key cause for the variability was that wealthy owners of farms and racetracks were willing and able to move their operations from one state to another. Kentucky's reemergence in the early 20th century as the leader in horse breeding was accompanied by increased dependence on professionals such as managers and trainers to oversee day-to-day operations of farms. Horse farms have also become more intertwined with local

economics through the farms' dependence on services such as specialized veterinary care and feed operations.

Trends In The Thoroughbred Breeding Industry

A key measure of the Thoroughbred breeding industry is the number of mares bred each year. Kentucky remains the dominant Thoroughbred breeding state, leading the nation in the number of Thoroughbred mares bred and the number of foals produced.

Since 1991, the number of Thoroughbred mares bred in the US has decreased by more than 40 percent. Comparatively, the number of mares bred in Kentucky demonstrated strong growth during the 1990s but has grown at a slower pace since 2000. Over the past 4 years, the numbers of mares bred in Kentucky, the US, and states other than Kentucky have declined.

Kentucky has captured a larger share of the Thoroughbred breeding market. The number of mares bred in the US has fallen as the number of mares bred in Kentucky has increased. During the past 2 decades, the percentage of US mares bred in Kentucky has continued to climb, reaching 43 percent in 2010.

The number of foals registered each year is commonly referred to as the foal crop. The trends in the foal crop for the US and Kentucky mirror the trends for the number of mares bred. Kentucky's share of the US foal crop has grown from 19 percent in 1991 to nearly 34 percent in 2010.

Staff compared Kentucky's annual foal crop to foal crops of six states that compete with Kentucky in the Thoroughbred breeding industry: Florida, Indiana, Louisiana, New York, Pennsylvania, and West Virginia. The annual foal crop in these six states increased over the past two decades, but the rate of growth was less than the growth in Kentucky's foal crop.

Thoroughbred Racing Industry

The Thoroughbred racing industry has experienced increasing competition from other forms of gaming such as lotteries and casinos. The racing sector grew during the 1990s as a result of off-track wagering, but in the past several years a weak economy and increased competition have led to nearly across-the-board declines in the racing sector.

Over the past decade, some states began to provide assistance to the industry. Assistance has been mainly in the form of breeders awards and purse supplements. West Virginia was the first state to use gaming receipts to supplement Thoroughbred purses. A number of states have followed suit by increasing their purse supplements with gaming receipts or a combination of revenue sources.

Kentucky's Programs To Assist The Equine Industry

Kentucky provides assistance to its horse breeding industry primarily by allocating the sales tax collected from stud fees to three breeders incentive funds established in 2006. The Kentucky Horse Racing Commission administers the funds. Eighty percent of the sales tax from stud fees is allocated to the Thoroughbred Breeders Incentive Fund, 13 percent is allocated to the Standardbred Breeders Incentive Fund, and 7 percent is allocated to the Horse Breeders Incentive Fund.

KRS 230.802(2)(b) directs the Kentucky Horse Racing Commission to promulgate administrative regulations for disbursing awards from the Standardbred Breeders Incentive Fund. No such regulations have been issued.

Recommendation 2.1

The Kentucky Racing Commission should promulgate administrative regulations establishing the conditions and criteria for the distribution of money from the Kentucky Standardbred Breeders Incentive Fund.

Awards from the breeders incentive funds are paid to breeders based on how their horses perform in races, shows, or contests. To qualify for an award, the foals produced by the horse breeder must be Kentucky sired, Kentucky bred, or both.

In fiscal year 2006, the breeders incentive funds received \$16.2 million. In the past 4 fiscal years, allocations to these funds have fallen as the number of mares bred and stud fees have declined. In FY 2011, \$11.6 million was distributed to the three funds.

Additional assistance is also provided to the horse industry via the pari-mutuel tax. A portion of this tax is dedicated to the Thoroughbred Development Fund, which provides purse supplements to the owners of Kentucky-sired, Kentucky-bred horses that win races in the commonwealth. The Standardbred Development Fund is also funded by a portion of the pari-mutuel tax. It and the Standardbred Breeders Incentive Fund serve as the funding source for purses for the Kentucky Sire Stakes series of Kentucky races for 2- and 3-year-old trotting and pacing fillies and colts. Revenue collected from the pari-mutuel tax has declined from more than \$18 million in FY 2000 to just less than \$11 million in FY 2011. As a result, less money has been allocated to the Thoroughbred Development Fund and the Standardbred Development Fund.

Economic Contribution

Kentucky's Thoroughbred breeding industry contributes to the state's economy directly through the workers it employs and expenditures by the farms to purchase products and services from other businesses. Staff used the survey results from Kentucky Thoroughbred farms and economic multipliers to estimate the contribution the Kentucky Thoroughbred breeding industry makes to Kentucky's economy.

Staff estimated that spending within the Thoroughbred breeding industry was approximately \$912 million in 2010. Due to this initial direct spending, total spending in Kentucky's economy that can be linked to the Thoroughbred industry was estimated to be \$1.58 billion.

In 2010, Kentucky's Thoroughbred breeding industry created about 10,800 jobs within the industry and 6,900 jobs in the ancillary sectors that provided goods and services to the industry. In total, more than 17,600 Kentucky jobs can be linked to the Thoroughbred breeding industry.

For every \$1 in earnings paid in the Thoroughbred breeding industry, an additional \$1.10 in earnings would be paid in other industries within the economy. Direct earnings paid in the Thoroughbred breeding industry in 2010 were estimated to be \$167.9 million. Total earnings associated with the industry were estimated to be \$352.7 million.

Chapter 1

Overview Of Kentucky's Horse Breeding Industry

The Program Review and Investigations Committee directed staff to study Kentucky's horse breeding industry and to examine how the Thoroughbred breeding industry affects the state's economy. This report describes the characteristics of Kentucky Thoroughbred farms, summarizes how the horse breeding industry developed in Kentucky, examines trends in the horse breeding market, analyzes how Thoroughbred breeding operations affect employment and earnings, and discusses Kentucky's efforts to promote the horse breeding industry. The study covers issues related to all breeds of horses, but portions focus primarily on the Thoroughbred breeding industry.

Kentucky still dominates the Thoroughbred industry, but increased competition from other states in the form of incentives offered to breeders and racehorse owners has narrowed the gap between Kentucky and these states. Competition with other states is not the sole factor affecting Kentucky's Thoroughbred industry.

A major factor affecting the industry is the long-term trend in declining handle due to competition from other forms of gaming and entertainment. In recent years, economic conditions have reduced the level of discretionary income of racetrack patrons and limited investment in many businesses, including the Thoroughbred industry.

Major Conclusions

This report has five major conclusions.

- Large farms are a small share of the total number of Thoroughbred farms but have large percentages of total horses and income.
- In 2010, Kentucky's Thoroughbred breeding industry created an estimated 10,800 jobs within the industry and 6,900 jobs in other sectors that support the industry and its workers.
- In 2010, Kentucky's Thoroughbred breeding industry contributed an estimated \$168 million in earnings from workers directly employed within the industry and \$185 million in earnings from workers employed in other sectors that support the breeding industry.

- Kentucky allocates sales tax revenue from stud fees to fund incentives for breeders and allocates a portion of the pari-mutuel tax to development funds that provide purse supplements to horse owners. Recent declines in breeding, stud fees, and pari-mutuel wagering have resulted in less available funding to support the equine industry.
- The number of Thoroughbred mares bred has declined in recent years in the US and in Kentucky, but Kentucky continues to gain a larger share of the nation's Thoroughbred breeding activity. A few other states are also gaining a share of the nation's breeding activity, but their shares are relatively small.

Characteristics Of Kentucky Thoroughbred Farms

In August and September 2011, staff surveyed members of the Kentucky Thoroughbred Owners and Breeders Association about their Kentucky farms.

Staff surveyed members of the Kentucky Thoroughbred Owners and Breeders Association about their Kentucky horse farms. The survey was conducted in August and September 2011.^a Of the 640 farms for which staff had valid addresses, 158 completed the survey, yielding a response rate of 25 percent. Appendix B contains the questionnaire and tabulated responses.

Nearly 40 percent of the surveyed Thoroughbred farms focused on breeding.

Table 1.1 shows surveyed Thoroughbred farms by type of operation. Thirty-nine percent of the farms were breeding operations, which kept studs or broodmares. The majority of these operations owned broodmares and their offspring. Approximately 23 percent of the farms were mainly commercial boarding operations, relying on boarding fees for income. Twenty-seven percent of the farms provided a wider range of services such as stud services, boarding, sales preparation, and training.

^a Staff compared results on acreage, number of horses, and employment from the 2011 survey to results from a 2001 survey conducted by the Kentucky Thoroughbred Owners and Breeders Association (Matrix). The results were similar.

Table 1.1
Surveyed Thoroughbred Farms By Type

Type Of Operation	Percent
Breeding	39.3%
Boarding	22.7
Diversified	27.3
Other	10.7
Total	100.0%

Note: 150 respondents. The reported type of operation is as of the time of the survey (August and September 2011).

Source: Staff survey of Thoroughbred farms.

About 47 percent of the horses on the farms were owned fully by the farm. Thirteen percent were owned partially by the farm. The remaining horses were owned by others and boarded at the farm.

Table 1.2 shows ownership of the horses at Kentucky Thoroughbred farms. Eighty-seven percent of the horses on these farms were broodmares, foals, weanlings, or yearlings. Of the horses at surveyed farms, 47 percent were fully owned by the farm and 13 percent were owned in partnership with others. Forty percent of the horses were boarded on the farms and owned by others.

Table 1.2
Horse Ownership At Surveyed Thoroughbred Farms

Ownership	Horses	Percent Of Total Horses
Owned fully by farm	3,972	46.9%
Owned partially by farm	1,105	13.0
Boarded for others	3,396	40.1
Total	8,473	100.0%

Note: 150 respondents. Reported ownership is as of January 1, 2011.
 Source: Staff survey of Thoroughbred farms.

Farm Size

One in six farms stood a stallion in 2010.

Survey respondents were asked to provide the number of stallions, mares, foals, weanlings, yearlings, 2-year-olds, and older horses on their farms in 2010. One of six farms stood a stallion. Typically, farms with stallions had 1 or 2 studs; however, 22 percent of these farms had 10 or more stallions. Survey respondents reported 114 stallions, which is equal to 41 percent of the stallions standing in Kentucky in 2010.

On average, farms had 32 broodmares.

Farms responding to the survey had on average 32 broodmares. Applying this average to the number of farms belonging to the Kentucky Thoroughbred Owners and Breeders Association suggests that there are more than 17,000 broodmares in Kentucky.^b

There were a relatively large number of small farms, but they accounted for a relatively small share of total horses. There were a few large farms that accounted for a larger share of total horses.

As shown in Table 1.3, numerous small farms accounted for a small share of the horses and a few large farms accounted for a large share of the horses. More than 63 percent of farms had 250 acres or less. These smaller farms accounted for 25 percent of the horses. About 7 percent of farms had more than 1,500 acres. These large farms accounted for about 34 percent of the horses. On average, farms covered 369 acres and had 59 horses.

Table 1.3
Acreege Of Surveyed Kentucky Thoroughbred Farms

Size In Acres	Percent Of Total Farms	Average Number Of Horses	Percent Of Total Horses
100 or less	33.3%	15	6.7%
101 to 250	29.9	51	18.3
251 to 500	18.8	65	20.5
501 to 1,499	11.1	106	20.5
1,500 or more	6.9	226	33.9
Total	100.0%		100.0%
Average: 369 acres, 59 horses			
Median: 175 acres, 32 horses			

Note: 141 respondents. The reported farm size is as of January 1, 2011. Percentages may not add to 100.0 due to rounding.

Source: Staff survey of Thoroughbred farms.

^b According to the Jockey Club, 17,165 mares were bred in Kentucky in 2010 (Fact Book: US).

About 34 percent of the farms accounted for 76 percent of the horses.

Table 1.4 shows the distribution of farms and horses based on the number of horses on each farm. Two-thirds of the farms each had fewer than 50 horses, accounting for 24 percent of the total horses. Only one-third of the farms had more than 50 horses each, but these farms accounted for 76 percent of the horses. Nearly half the Thoroughbreds were on the 12.6 percent of farms that each had more than 100 horses.

Table 1.4
Horses Per Surveyed Thoroughbred Farm In 2010

Horses	Percent Of Total Farms	Percent Of Total Horses
20 or fewer	35.0%	5.6%
21 to 50	31.4	18.7
51 to 100	21.0	26.7
More than 100	12.6	49.0
Total	100.0%	100.0%

Note: 141 respondents. The number of horses is the reported daily average for 2010.

Source: Staff survey of Thoroughbred farms.

Farm Employment

Most of the employees at Thoroughbred farms worked full time. About 22 percent worked either part time or seasonally.

Thoroughbred farms are relatively labor-intensive operations requiring diverse skills. Employees are needed to perform general farm upkeep, provide basic horse maintenance, and provide specialized skills associated with managing stallions and breeding mares. Seventy-eight percent of the employees on surveyed Thoroughbred farms in 2010 were full-time, year-round employees, and 22 percent were part-time or seasonal employees. Table 1.5 summarizes full-time employment on the surveyed farms. More than one-third of the farms each had fewer than 3 full-time employees, 62 percent had 5 or fewer, and 75 percent had fewer than 10. Nearly 11 percent of farms each had more than 25 employees.

Table 1.5
Full-Time Employees Per Surveyed
Thoroughbred Farm In 2010

Employees	Percent Of Total Farms
0 to 3	37.7%
3 to 5	24.6
6 to 10	12.3
11 to 25	14.6
26 to 100	8.5
More than 100	2.3
Total	100.0%

Note: 117 respondents. Reported employees are for 2010. Ten farms (7.7 percent) among these respondents reported no full-time employees.

Source: Staff survey of Thoroughbred farms.

On average, farms had about 13 full-time employees and 4 part-time or seasonal employees.

The farms employed 1,727 full-time employees in total in 2010 and maintained 8,473 horses, which was 4.9 horses per full-time employee. The average number of full-time employees was 13.3, and the median number of employees per farm was just under 4. As farm size increased, the number of horses per employee declined.

Almost three-quarters of the Thoroughbred farms had part-time or seasonal employees. On average, farms had four part-time or seasonal employees per farm, but this measure was heavily influenced by the number of part-time or seasonal employees on large horse farms. Most of the farms that used part-time or seasonal employees—68 percent—had one or two employees who worked for almost 6 months. Based on the survey responses, many of these employees would be classified as full-time seasonal employees because they worked at least 40 hours per week.

Farm Income

Twenty percent of the Thoroughbred farms accounted for nearly 84 percent of the income earned by farms.

Table 1.6 shows that most of the income reported by surveyed Thoroughbred farms was concentrated among a relatively small percentage of the farms. Forty-three percent of the farms each reported gross income of less than \$250,000, which together accounted for only 2.5 percent of the income earned by all of the surveyed farms. For 20 percent of the farms, gross income of more than \$1 million each was reported, accounting for nearly 84 percent of the total income earned by the surveyed farms.

Table 1.6
Annual Income Per Surveyed Thoroughbred Farm In 2010

Income	Percent Of Total Farms	Percent Of Total Income
\$250,000 or less	43.2%	2.5%
\$251,000 to \$500,000	16.2	3.7
\$500,001 to \$1,000,000	20.4	10.0
More than \$1,000,000	20.2	83.8
Total	100.0%	100.0%

Note: 118 respondents.

Source: Staff survey of Thoroughbred farms.

Thoroughbred farms earn income by standing stallions, selling weanlings and yearlings, boarding horses, and other activities.

Thoroughbred farms generate revenue based on the production activities that take place on the farm. Farms that stand stallions earn stud fees. Breeding farms generate revenues from selling weanlings and yearlings but also earn revenue by boarding horses. Farms also earn income from other sources such as sales preparation fees, training fees, and sales commissions.

Twenty-four percent of Thoroughbred farms' income came from horse sales.

Table 1.7 summarizes the Thoroughbred farms' income by source. Total gross income for the 118 farms that responded to this question was \$183.1 million in 2010. The surveyed farms earned \$55.6 million in stud fees, which was 30.4 percent of the total income earned by these farms. Approximately 15 percent of the farms received income from stud fees. The vast majority of these farms had only one or two studs, bred fewer than 150 mares per year, and earned less than \$500,000 in stud fees. The larger stud farms had 10 or more studs and bred more than 1,000 mares in 2010.

Almost one-quarter of the income earned by the farms surveyed came from equine sales, and nearly 23 percent came from boarding fees. Sales commissions, sales preparation, and training and management fees accounted for 5.7 percent of income.

Farms with less than \$100,000 in gross income were less diversified and were highly dependent on sales in the commercial market. They did not generate substantial income from boarding, sales commissions, sales preparation, or stud fees.

Table 1.7
Sources Of Income For Surveyed Thoroughbred Farms In 2010

Source Of Income	Gross Income (\$ millions)	Percent Of Gross Income
Equine sales	\$44.0	24.0%
Stud fees	55.6	30.4
Boarding fees	41.6	22.7
Commissions, sales preparation, training and management fees	10.4	5.7
Other	31.4	17.1
Total	\$183.1	100.0%

Note: 118 respondents. Income and percentages do not add to totals shown due to rounding.

Source: Staff survey of Thoroughbred farms.

Thoroughbred farms indicated they sold 1,128 horses in 2010 for an average price of \$91,000 per horse.

Of the foals that are born in a particular year, a small percentage are sold as weanlings, a much larger percentage are sold as yearlings, and some are sold as 2-year olds. Sales of these horses are an important source of income for the farms. Farms sell horses they own and also serve as sales agents for owners of other horses. Survey respondents sold 1,128 foals for \$102.7 million in 2010. A portion of this amount represents income for the farm; the remainder is income for the owner of the horse. The average price received per horse was \$91,000.^c Table 1.8 shows sales income per horse for farms of different sizes. Generally, sales income per horse was higher for larger farms. The exception was farms with more than 1,000 acres, which earned less per horse than farms with 251 to 1,000 acres.

Table 1.8
**Sales Income By Farm Size For
Surveyed Thoroughbred Farms In 2010**

Size In Acres	Sales Income Per Horse
Less than 100	\$20,476
101 to 250	29,328
251 to 500	157,740
501 to 1000	167,395
More than 1,000	105,059

Note: 93 respondents.

Source: Staff survey of Thoroughbred farms.

^c The average price for weanlings, yearlings, and 2-year-olds from the survey is higher than the \$64,811 average price paid for yearlings purchased at the Keeneland September yearling sales in 2010 (Blood-Horse).

The surveyed farms earned approximately \$82 per horse net of expenses.

Total expenditures in 2010 for the surveyed farms were \$182.4 million, which is close to the total income of \$183.1 million. However, eight farms reported expenditures but did not report income. Staff calculated the average income per horse and the average expenditure per horse for the respondents. The average income per horse was \$21,613, and the average expenditure per horse was \$21,531. The net income was \$82 per horse, yielding a 0.38 percent return over expenses.^d

How Kentucky Became The World Horse Breeding Capital

Prior to the Revolutionary War, New York and Maryland were the centers of horse racing interests. When gentry horsemen began moving into the Bluegrass region of Kentucky after the war, most of the early Kentucky farms raised a variety of livestock and breeding was a side issue, with little thought given to pedigree (Domer).

Kentucky horse racing grew during the early and middle parts of the 19th century.

As Kentucky's horse racing industry grew during the early and middle parts of the 19th century, some of central Kentucky's wealthier farmers placed more emphasis on raising racehorses (Domer). Robert A. Alexander's Woodburn Farm in Woodford County opened in 1849 and served as the foundation on which Kentucky's legacy as the horse capital of the world would be built (Wall).

Woodburn was one of the first American farms to keep pedigree records for all its horses. Alexander used the records to select breeding pairs in an attempt to improve the quality of the offspring (Domer). Alexander gained an international reputation as the most talented breeder in the nation.

By the early 1860s, Alexander and a handful of local competitors, such as Nanutra Stud, Stone Wall Farm, and Bosque Bonita Farm, had put central Kentucky on the map as one of the best places in the country for breeding and raising high-quality bloodstock. Kentucky was also garnering national attention because of Woodburn Farm's annual sales, which drew horse enthusiasts, breeders, and media from all over the country (Wall).

A contributing factor to Kentucky's rise to the top of the horse industry was the impact of the economic downturn on horse-breeding operations in the Northeast in the 1840s. During a period

^d An analysis was done by farm size that compared income to expenditures. There was no strong pattern in the data.

of runaway inflation and the collapse of many financial institutions, the Northeast saw a decline in public support for gambling in general, and horse racing in particular. By the 1840s, New York's horse breeding industry had all but collapsed and racetracks struggled to find enough horses to fill their race cards. This provided Kentucky horsemen with the opportunity to sell their horses and to showcase the quality of their product (Wall).

The quantity and quality of Kentucky's bloodstock dramatically declined during the Civil War because of military conscription and thievery. Kentucky lost a large portion of the commercial horse market when most southern racetracks closed. Then, Kentucky's horse industry lost a large portion of its labor force at the end of the war, as freed slaves moved off the farms and into cities. Many Kentucky horse farms went bankrupt because of the war.

As Kentucky struggled to keep its horse-breeding industry alive, a small group of Wall Street tycoons and wealthy bankers from the Northeast revived horse racing in New York and New Jersey. Men such as William R. Travers, James R. Keene, and August Belmont invested their own money to construct extravagant horse farms and lavish racetracks such as Saratoga. By the late 1870s, their efforts had reawakened public interest in horse racing. Once they began retiring their best horses to breeding careers on their own farms, they had little need for Kentucky-bred horses.

By the 1880s, some 300 racetracks were operating across the United States. Breeders looked to states other than New York and New Jersey for high-caliber horses, which would eventually help renew Kentucky's importance to horse breeding.

Beginning in 1885, many prominent horsemen moved their breeding operations to Kentucky.

In 1885, August Belmont moved his New York breeding operation, Nursery Stud, to Lexington. Belmont's move to Lexington brought attention and money to the state's struggling horse industry. Following his lead, several other wealthy horsemen eventually moved their breeding operations to Kentucky.

During the 1890s, as Kentucky's horse industry was reemerging, horse racing elsewhere was affected by the wave of Progressive Era reforms limiting perceived vices such as gambling. Horse racing was largely banned in every state except Kentucky and Maryland. In 1897, 314 racetracks operated in the United States; by 1908 there were 25 (Liebman).

Between about 1890 and 1920, most horse breeders had to struggle to keep their operations afloat. It was during this period that many breeders turned to Kentucky and found great success. James A.

Keene purchased Castleton Farm in 1892, and by 1912 he had bred more than 100 stakes winners. Edward R. Bradley founded Idle Hour Farm in 1906 and would eventually own or breed four Kentucky Derby winners. In 1910 near Paris, Arthur B. Hancock started Claiborne Farm, which he and his sons would parlay into a breeding dynasty. August Belmont's son had a horse that foaled Man o' War at the Nursery Stud farm in Lexington.

In the 20th century, the horse breeding and racing businesses became more intertwined with the local economy. Professional horsemen such as managers and trainers handled day-to-day operations. Businesses such as veterinary specialists and horse feed operations emerged to support the growing Kentucky horse industry.

Kentucky's return to prominence during the early part of the 20th century was accompanied by a change in how the state's horse industry operated. Nineteenth-century horse farm owners had played an integral role in running their farm, but many of the new owners rarely visited their farms. They relied on a new class of workers—the professional horsemen—to run their day-to-day operations. These professional horsemen included specialists such as farm managers, bloodstock agents, and trainers. Additionally, many ancillary businesses, such as veterinary specialists, horse feed operations, and banking and insurance services, emerged to meet these farms' needs. As successive farms opened, the business of breeding and raising racehorses became more intertwined with local economies. The emergence of the professional horsemen provided the state's horse industry with the necessary support to develop its horse breeding industry.

Geology

The limestone in central Kentucky is associated with land that is rich in calcium and phosphorus, which are important to a horse's development. Mare owners in the state indicate that the land, soil, and forages that are unique to Kentucky are important to them.

The rolling terrain and the geology of the Bluegrass region, particularly its limestone, are believed to provide the commonwealth with a natural advantage in raising and breeding horses. Specifically, Middle Ordovician limestone, which formed between 490 million and 438 million years ago in the central part of the state, is associated with land that is rich in calcium and phosphorus. Many minerals are important in the development of a horse, but calcium helps horses develop bones and phosphorus is a significant component of a horse's bones. Phosphorus also plays a vital role in the production of energy within a horse. Horses grazing on limestone-based land may benefit from higher concentrations of these minerals.

Fertile pastureland is just one of the factors horse owners consider when deciding where to raise horses, but the second most mentioned asset by respondents to a 2011 study was the land, soil, and forages of the state. (The group indicated that the availability of top stallions was Kentucky's greatest advantage.^e) During farm

^e The Kentucky Thoroughbred Association and the Kentucky Thoroughbred Owners and Breeders Association commissioned the survey by the Matrix Group (Matrix).

interviews staff conducted as part of this Program Review study, all farm owners indicated that their clients value the quality of the forages available in Kentucky and all owners indicated that they valued their rich pastures and intensively managed them to produce the best horses possible.

Trends In Thoroughbred Breeding

Mares Bred

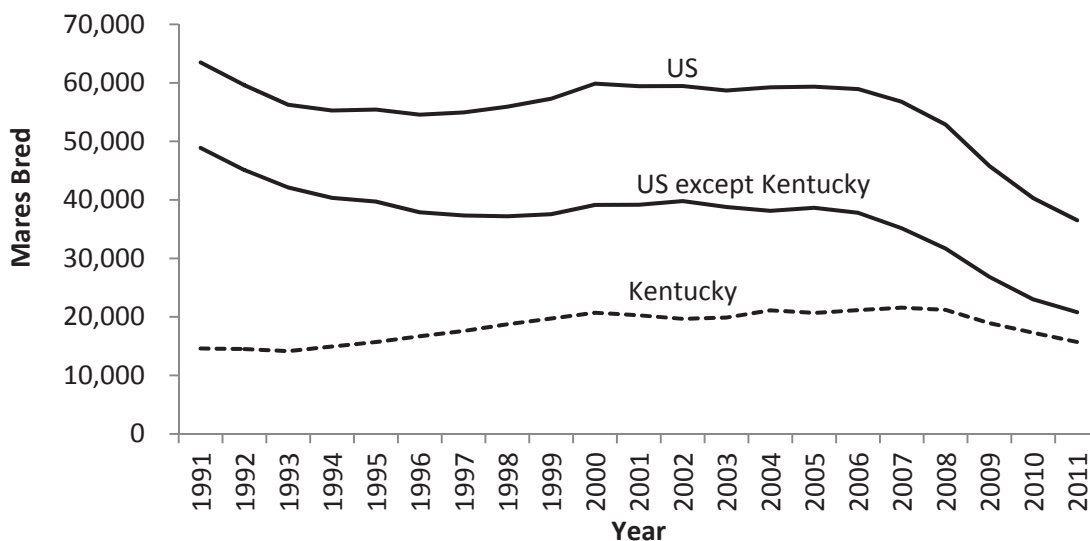
The number of mares bred annually is a key measure of the Thoroughbred Industry.

A key measure of the Thoroughbred breeding industry is the number of mares bred annually. This and the conception and foaling rates determine the size of the Thoroughbred foal crop the year after the mares are bred.

Nationally, the number of mares bred decreased during the early 1990s but increased from 1993 to 2000.

Figure 1.A shows the annual number of Thoroughbred mares bred in Kentucky, other states, and the US as a whole from 1991 to 2011. In 1991, more than 63,000 Thoroughbred mares were bred in the US. The number of Thoroughbred mares bred in the nation declined during the early 1990s, in part because of lingering effects of the national recession, large foal crops in earlier years, and tax changes relating to passive activity losses.

Figure 1.A
Thoroughbred Mares Bred In The US
1991 To 2011



Source: Compiled by staff from Jockey Club. "Fact Book: US."

As economic conditions improved, Thoroughbred yearling prices increased from 1993 until 2000. With improving market conditions, the number of mares bred in the US rebounded and reached 60,000 by 2000. The gains in the number of mares bred in the later part of the 1990s did not fully offset the losses that occurred earlier in the decade.

The number of mares bred has declined since 2007. By 2011, the number for the US had declined by 42.5 percent when compared to 1991.

After 2000, Thoroughbred breeding activity in the country remained steady through 2006 but then started to decline. Since 2007, the number of mares bred has fallen and the rate of decline has accelerated. From 1991 to 2011, the number of mares bred in the US per year fell by almost 27,000, a 42.5 percent decrease.

The number of mares bred in Kentucky demonstrated strong growth from 1994 to 2001.

Beginning in 1994, for each of the next 7 years the number of mares bred in Kentucky grew, reaching 20,713 in 2000. This represents a 42 percent increase from 1991 and was much greater than the increase for the US during this period.

Kentucky breeding declined in 2001 and 2002 as a result of mare reproductive loss syndrome, which caused many of the mares in Kentucky to lose their foals.

The rapid growth in the number of mares bred ended in 2001. In the spring of 2001, veterinarians in the state reported that an unusually large number of broodmares were unexpectedly losing their foals during the late stages of gestation. These late-term losses were foals that were born dead or sick and were from mares bred in 2000 that were carrying a full-term foal in 2001. Later in the 2001 breeding season, mares that were bred in 2001 started to experience early term fetal losses. These two losses reduced the number of foals born in Kentucky in 2001 and 2002 and reduced the number of mares bred in 2001.^f The cause of these losses was later named mare reproductive loss syndrome.

From 2003 to 2007, Kentucky's breeding activity improved. Since 2007, the number of mares bred in Kentucky has declined.

After declining in 2001 and 2002, the number of mares bred in Kentucky increased again, but at a slower pace than in the 1990s. Intermittent growth in the number of mares bred in Kentucky from 2002 to 2007 was followed by annual declines in each of the past 4 years. Since 2007, the number of mares bred in Kentucky has declined but at a slower rate than in the US.

Breeding in states other than Kentucky has generally declined since 1991.

In Figure 1.A, the difference in the number of mares bred in Kentucky and the rest of the US is indicated by the gap between the two trend lines. Since 1991, the difference in these two measures has narrowed, indicating fewer mares are being bred

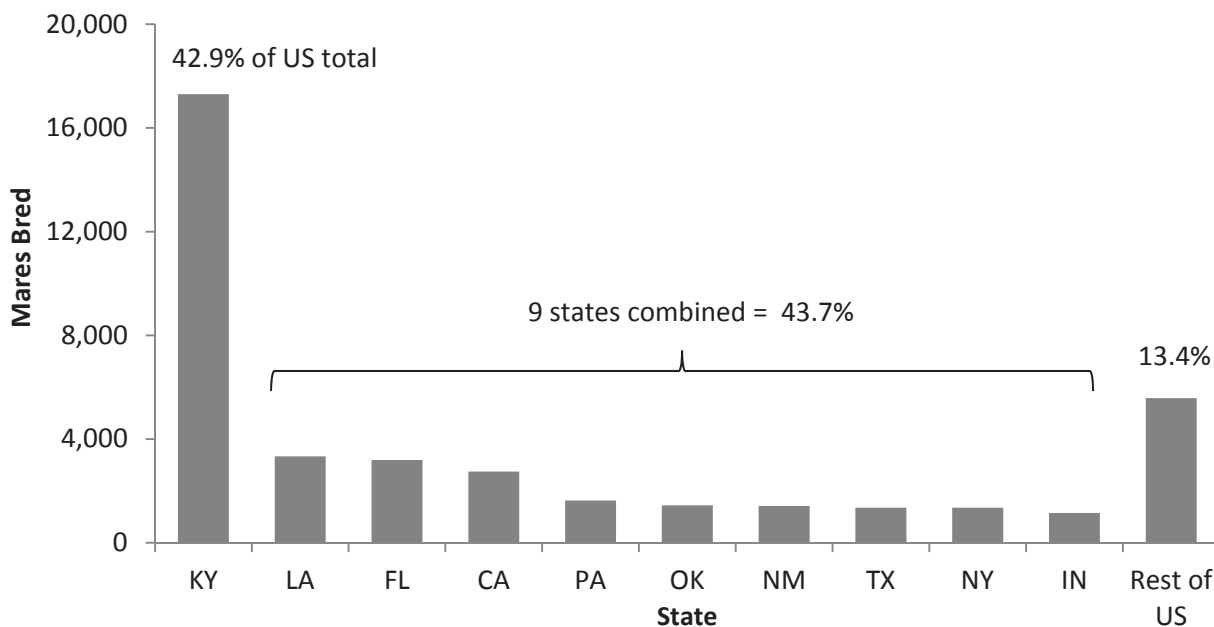
^f Breeding activity in the state in 2001 was affected for two main reasons. Mares that had lost foals in 2001 were reported as cycling and some were rebred and in foal, but rebreeding was often not successful. Also, many of the early-term losses were 30 to 45 days after cover, by which time the traditional end of the breeding season had passed (Thalheimer).

outside of the state relative to the number of mares bred in Kentucky. The number of mares bred in Kentucky in 2011 was 7.7 percent higher than the number bred in 1991. In other states, the number of mares bred was 57.5 percent lower than in 1991.

Kentucky remains the dominant state within the Thoroughbred breeding industry, accounting for 43 percent of Thoroughbred mares bred in the US in 2010.

Kentucky remains the dominant state within the Thoroughbred industry. Figure 1.B shows the number of mares bred in 2010 in Kentucky, the rest of the US, and the remaining top 10 states: California, Florida, Indiana, Louisiana, New Mexico, New York, Pennsylvania, Oklahoma, and Texas. Kentucky led the nation in 2010 with 17,303 mares bred out of a total 40,293. The number of mares bred in the remaining top 10 states in 2010 was 17,604. That is, 9 of the top 10 states combined bred slightly more Thoroughbreds than Kentucky. Almost 43 percent of mares bred in the nation in 2010 were bred in Kentucky, 43.7 percent were bred in the other top 10 states, and 13.4 percent were bred in the remaining 40 states.

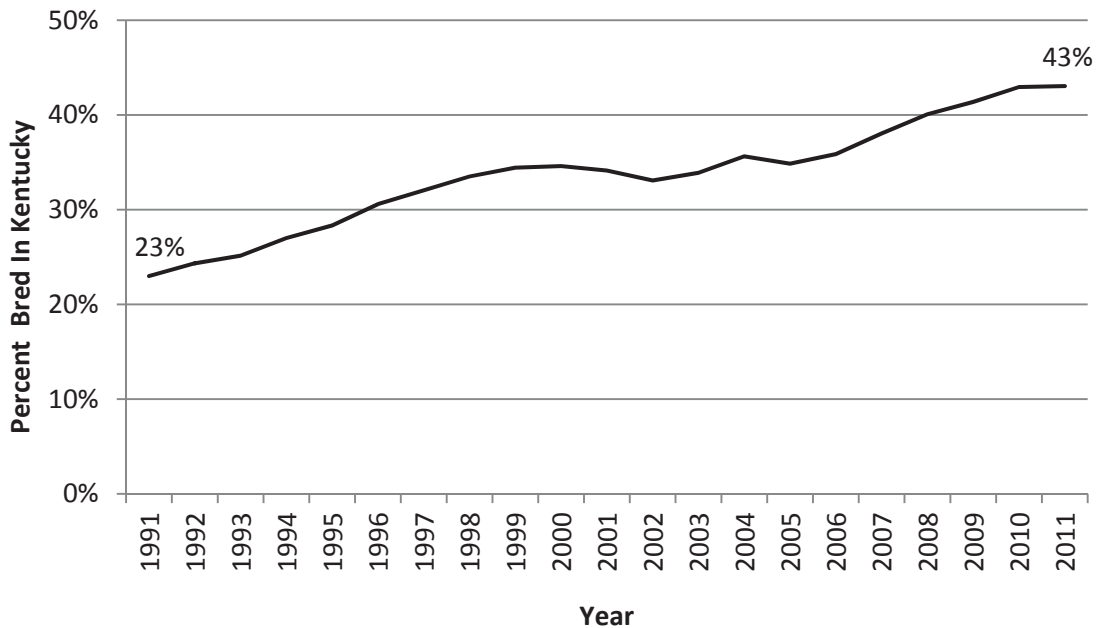
Figure 1.B
Thoroughbred Mares Bred In 2010



Source: Compiled by staff from Jockey Club. "Fact Book: US."

Figure 1.C shows the increase in the percentage of the nation's mares that are bred in Kentucky. In 1991, 23 percent of the nation's mares were bred in Kentucky. By 2000, Kentucky's share increased to 34.4 percent. After the 2-year period when Kentucky was affected by mare reproductive loss syndrome, Kentucky continued to gain a larger share of the US market. Kentucky's share of the market now stands at 43 percent.

Figure 1.C
Percentage Of US Thoroughbred Mares Bred In Kentucky
1991 To 2011



Source: Staff calculations based on Jockey Club. "Fact Book: US."

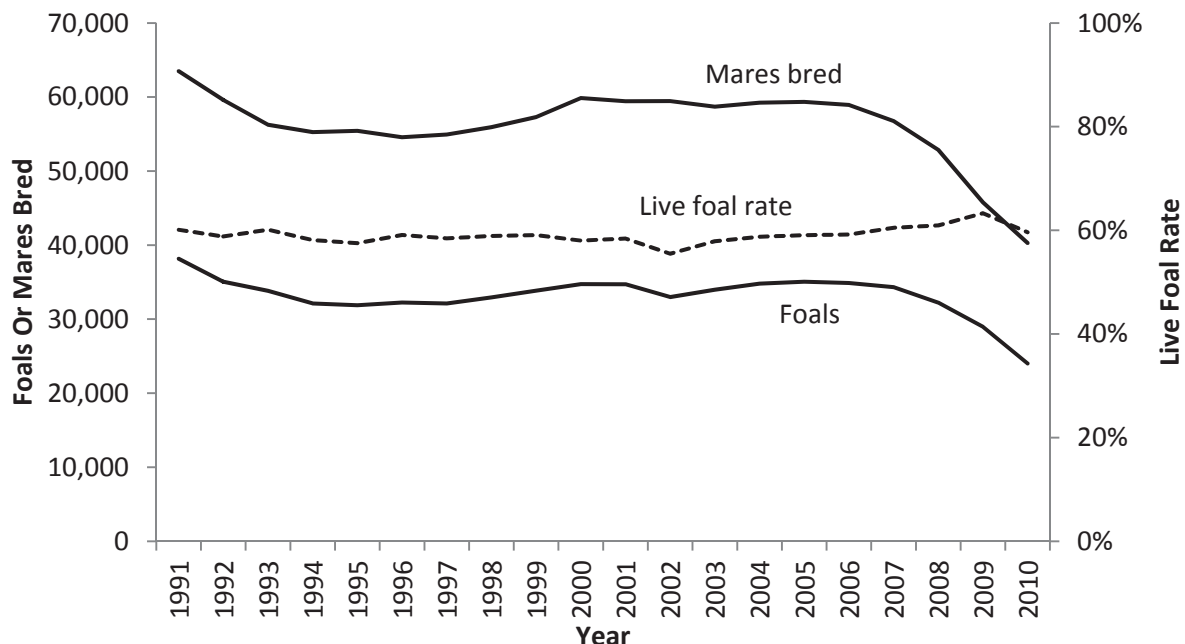
Foals

Annual foal production is directly related to the number of mares bred in the previous year. The difference between the number of mares bred in one year and the foals produced in the following year is due to conception and foal rates. Typically, 60 percent of mares bred produce a live foal. The number of foals produced will be less than the number of mares bred, but the trends in these two measures will mirror one another.

Nationally, the number of registered Thoroughbred foals has declined in recent years.

Figure 1.D displays the number of mares bred, the number of registered foals, and the live foal rate for the US from 1991 to 2010. Over the past 10 years, the number of Thoroughbred foals registered in the US has generally varied between 32,000 and 35,000 annually. However, recent estimates of the number of registered foals indicate this number dropped below 30,000 in 2009 and will decline further in 2010.

Figure 1.D
Mares Bred, Foals, And Live Foal Rate In The US
1991 To 2010



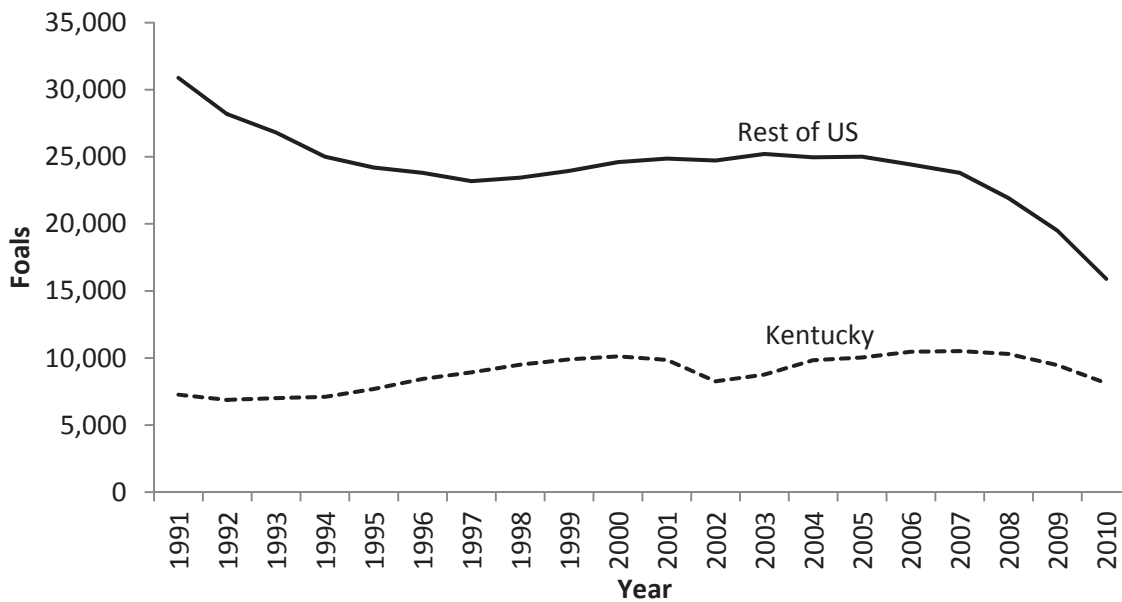
Note: The number of foals for 2010 is an estimate.

Source: Compiled by staff from Jockey Club. "Fact Book: US." and "Fact Book: Distribution."

In Kentucky, the number of registered foals has remained close to 10,000 since 1999 but has declined in recent years.

At the state level, the trend in the number of foals may not follow the trend in the number of mares bred because a mare may be bred in one state but may foal in a different state. Figure 1.E displays the number of Thoroughbred foals in Kentucky and other states. With the exception of the 2 years affected by mare reproductive loss syndrome, approximately 10,000 Thoroughbred foals were born annually in Kentucky from 1999 to 2008. The number of foals in Kentucky declined to 9,470 in 2009 and is estimated to fall further in 2010. The number of foals in states other than Kentucky has been close to 25,000 per year since 1999. Recent data indicate the number of foals in other states started to decline prior to the decline in Kentucky.

Figure 1.E
Foal Crop In Kentucky And Rest Of US
1991 To 2010



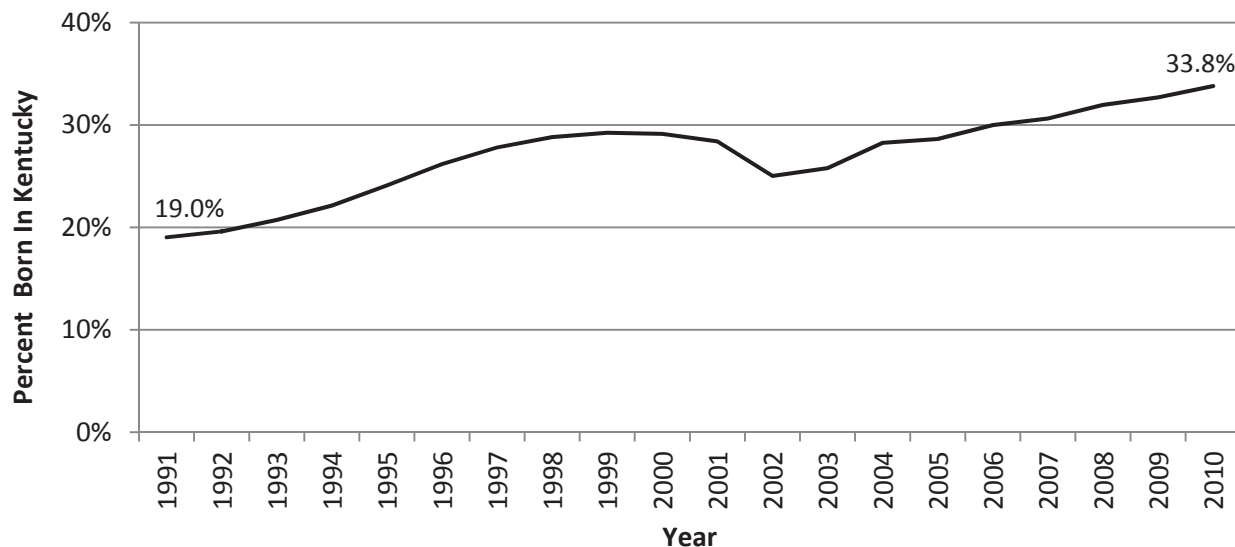
Source: Compiled by staff from Jockey Club. "Fact Book: Distribution."

While the total number of mares bred has declined in both the nation and Kentucky, Kentucky's share of the US foal crop has increased.

During the 1990s, the number of foals in Kentucky increased while the number of foals in other states declined. After the 1990s, the foal crop in Kentucky and in the other states held steady. Recent data indicate a further narrowing of the difference between the number of foals outside Kentucky and the number of foals in the state.

As with the number of mares bred, Kentucky's share of the annual foal crop is growing, as shown in Figure 1.F. In 1991, 19 percent of foals were born in Kentucky. By 2010, Kentucky's share of the foal crop grew to 33.8 percent.

Figure 1.F
Kentucky's Percentage Of US Foal Crop
1991 To 2010



Source: Compiled by staff from Jockey Club. "Fact Book: Distribution."

Competing States

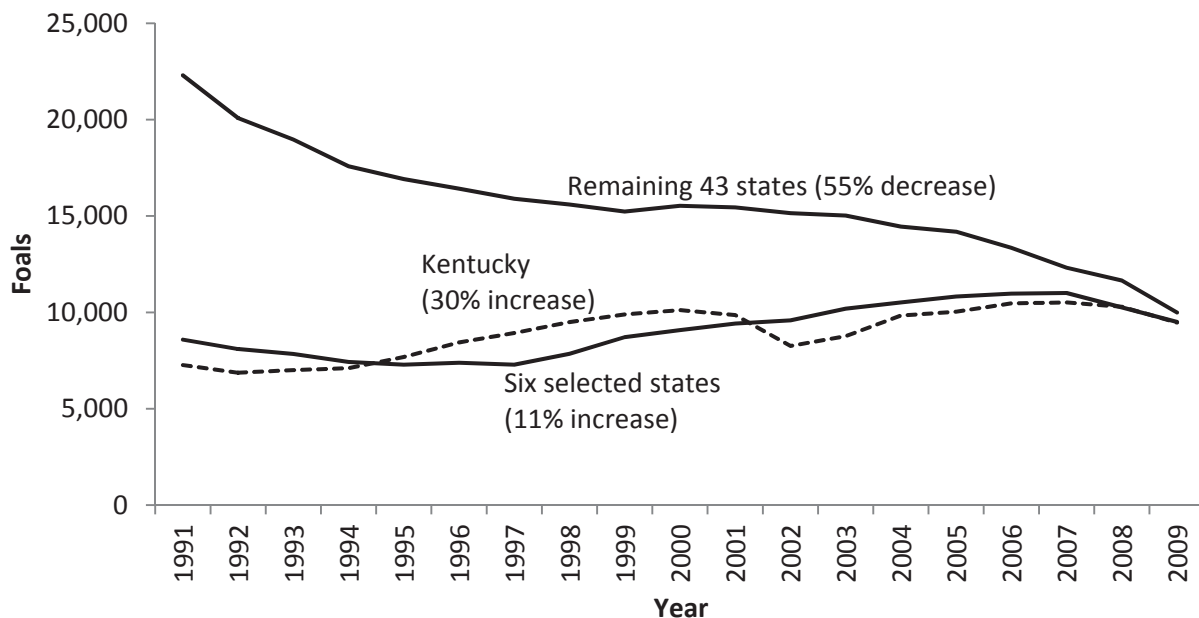
Staff selected six states that compete with Kentucky's Thoroughbred breeding industry: Florida, Indiana, Louisiana, New York, Pennsylvania, and West Virginia.

The number of foals born in other states relative to the number born in Kentucky has declined, but this relationship has not held for all states for all years. Figure 1.G compares trends in the total number of foals in Kentucky, 6 competing states, and the 43 remaining states. The competing states Florida, Indiana, Louisiana, New York, Pennsylvania, and West Virginia were selected because they are relatively close to Kentucky, they provide incentives to the horse industry, and they compete with Kentucky for Thoroughbred breeding. The number of foals in Kentucky and the six selected states has varied but generally has increased. In the 43 remaining states, the number of foals declined by 55 percent.

The number of mares bred in these six states, as a group, increased from 1997 but has declined in recent years.

Overall, from 1991 to 2009, the number of foals born in Kentucky has grown faster than in the six selected states. However, in some years, the number of foals born in the six selected states exceeded the number born in Kentucky. From 1991 to 1997, the number of foals grew faster in Kentucky. From 1997 to 2002, growth in the selected states exceeded growth in Kentucky. After 2002, the number of foals born in Kentucky increased again and the rate of growth has exceeded the growth rate for the selected states. In 2008 and 2009, however, the number of foals in Kentucky and in the group of selected states has declined.

Figure 1.G
Foals Born In Kentucky, Six Selected States, And Remaining States
1991 To 2009

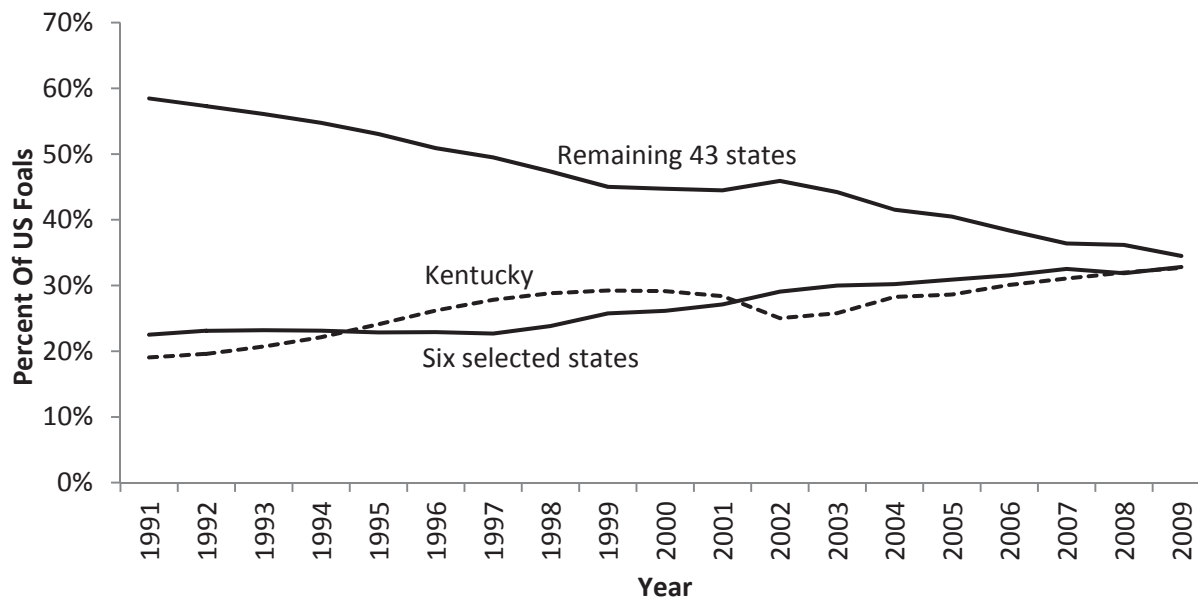


Note: The six selected states are Florida, Indiana, Louisiana, New York, Pennsylvania, and West Virginia.
 Source: Compiled by staff from Jockey Club. "Fact Book: Distribution."

The percentage of the nation's foals born in Kentucky and the six states as a group has increased.

Figure 1.H shows the share of foals born in Kentucky, the selected states, and the rest of the US. In 1991, 19 percent of the nation's foals were born in Kentucky, 22.5 percent were born in the selected states, and 58.5 percent were born in the 43 remaining states. Over time, Kentucky and the selected states have accounted for a larger share of the nation's foals. Kentucky, the group of selected states, and the group of remaining states in the US as a group now account for one-third each of the nation's foals. The data indicate that Kentucky has gained market share and still accounts for the largest share of the foals but that its competitor states, as a group, have also gained market share.

Figure 1.H
Percentage Of Foals Born In Kentucky, Six Selected States, And Remaining States
1991 To 2009



Note: The selected states are Florida, Indiana, Louisiana, New York, Pennsylvania, and West Virginia.

Source: Compiled by staff from Jockey Club. "Fact Book: Distribution."

Of the foals that were sired in Kentucky in 2009, 32 percent were foaled outside Kentucky.

As shown in Table 1.9, most mares bred to a Kentucky stallion foal in Kentucky, but some foal outside the state. In 2005, 30.5 percent of the foals that were sired in Kentucky were born in another state. By 2009, this figure had increased slightly to 32.4 percent. Some of these foals are born in the six selected states Kentucky competes against. The percentage of Kentucky-sired foals born in one of the selected states increased from 14.4 percent in 2005 to 16.5 percent in 2009.

Table 1.9
Foaling Area Of Kentucky-Sired Registered Foals
2005 To 2009

Year	Foaled In Kentucky	Foaled Outside Kentucky
2005	69.5%	30.5%
2006	70.2	29.8
2007	70.0	30.0
2008	68.5	31.5
2009	67.6	32.4

Source: Calculated by staff from Jockey Club. 2011.

Trends In The Thoroughbred Racing Industry

Trends in the Thoroughbred breeding industry are tied to trends in the Thoroughbred racing industry, which has undergone significant changes in the past two decades.

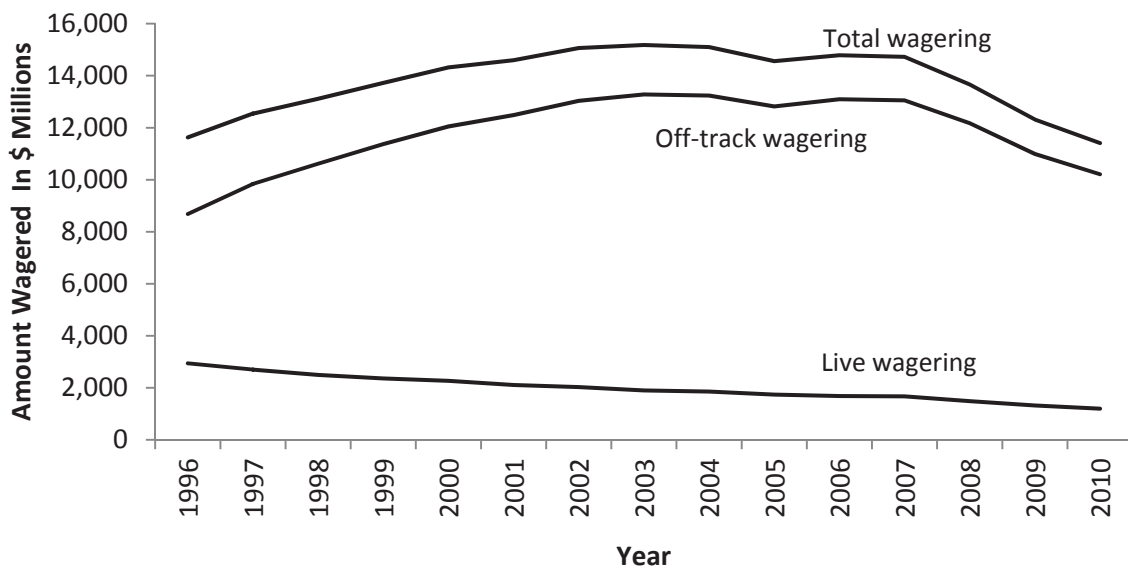
The Thoroughbred breeding industry has experienced an across-the-board decline since the beginning of the recession.

As competition has increased and economic conditions over the past 3 years deteriorated, the Thoroughbred industry has experienced a nearly across-the-board decline as measured by barometers such as race days, attendance, handle, purses, mares bred, and stud fees. Exceptions are the recent improvement in public auction yearling prices and the increasing support in some states in the form of purse supplements and breeder’s awards.

Off-track wagering provided the stimulus for growth in the Thoroughbred breeding industry in the 1990s.

Figure 1.I shows the amount of live wagering, off-track wagering, and total wagering on Thoroughbred races from 1996 to 2010. Off-track wagering includes wagering at off-track betting facilities and simulcast wagering. Data were unavailable prior to 1996, but the trends suggest that growth in off-track wagering in the 1990s through 2003 drove the growth in total wagering. From 1996 to 2010, live wagering declined steadily. Off-track wagering allowed the industry to reach new customers and provide previous customers with more opportunities to wager.

Figure 1.I
US Thoroughbred Pari-Mutuel Wagering
1996 To 2010



Source: Jockey Club. “Fact Book: Pari-Mutuel.”

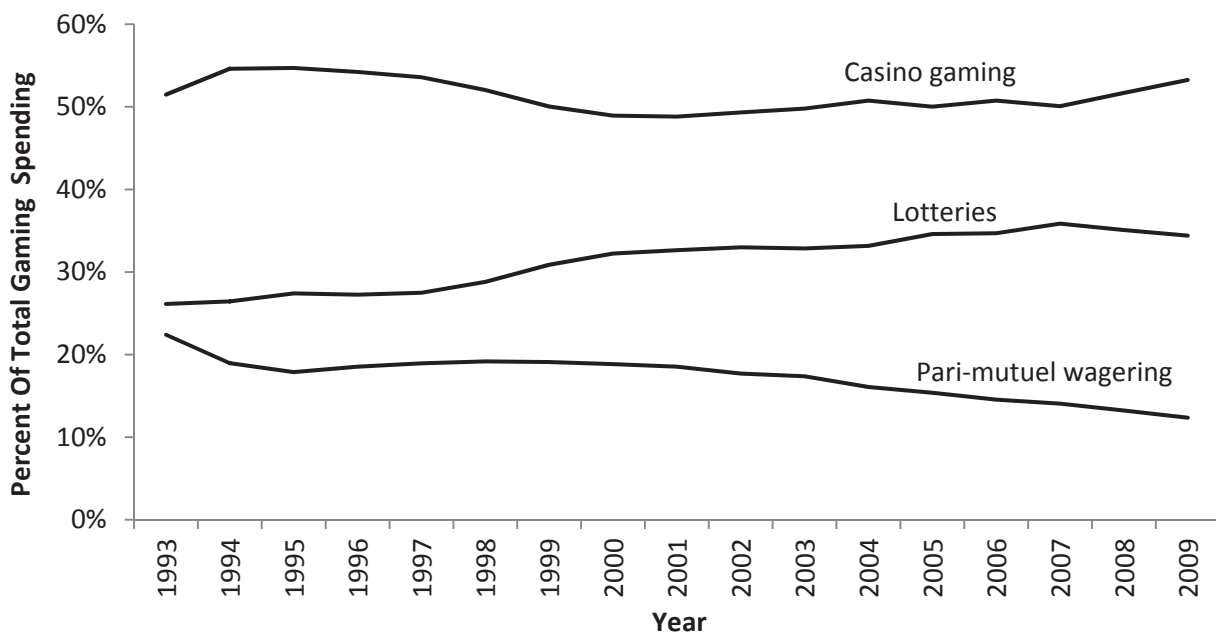
US wagering grew by 58 percent from 1991 to 2003 but has declined in 6 of the past 7 years.

In the 1990s, total Thoroughbred pari-mutuel wagering increased as the total number of races declined. US wagering grew by 58 percent from 1991 to 2003 but has declined in 6 of the past 7 years as the growth in off-track wagering leveled off. Over the past 4 years, total wagering on Thoroughbred races in the US has fallen by 23 percent, and purses for Thoroughbred races have fallen by almost 13 percent since the recession began in December 2007.

US consumers are showing an increased preference for other types of gaming.

Over the past 2 decades, more states have adopted lotteries and authorized casino gaming, and US consumers have shown an increased preference for other types of gaming. As shown in Figure 1.J, pari-mutuel wagering on Thoroughbred races has declined as a percentage of the total consumer dollars spent on gaming activities.

Figure 1.J
Consumer Spending On Thoroughbred Pari-Mutuel Wagering, Lotteries, And Casino Gaming In the US 1993 To 2009



Source: American Jockey Club. "Fact Book: Pari-Mutuel"; US. Census.

The Thoroughbred breeding industry is highly dependent on capital investment.

The performance of the US and Kentucky Thoroughbred industry is closely tied to changes in the national economy. The industry requires and is highly dependent on capital investment in bloodstock: the mares that produce the foals and the yearlings purchased by racehorse owners. Whether one owns horses to breed or to race, participation in the industry requires an investment in

which there is often only a small chance of a payoff, and the returns, if any, come after years of spending on upkeep, care, and training. Therefore, when the economy and financial markets tighten, investment in the industry contracts as investors either can no longer incur losses or move to safer assets. Much of the industry is affected by the level and changes in discretionary income, from the horse owners' and horse breeders' investment in bloodstock to fans' betting on races.

As the Thoroughbred industry faced increasing competition, some states began to provide assistance to the industry.

As the Thoroughbred industry faced increasing competition, some states began to provide assistance to the industry, largely in the form of breeder's awards and purse supplements. The resources to fund these incentives typically come from pari-mutuel taxes, unclaimed winnings, breakage, states' general funds, and gaming receipts.^g

West Virginia was the first state to use gaming receipts to supplement Thoroughbred purses. Other states have followed suit with purse supplements tied to gaming receipts or to a combination of revenue sources.^h As states have taken actions to boost their breeder's awards and purses, competition has increased between the states for the money spent by Thoroughbred mare and racehorse owners.

Figure 1.K shows total purses, the amount of total purses derived from handle or wagering at the track, and the amount of total purses derived from purse supplements.

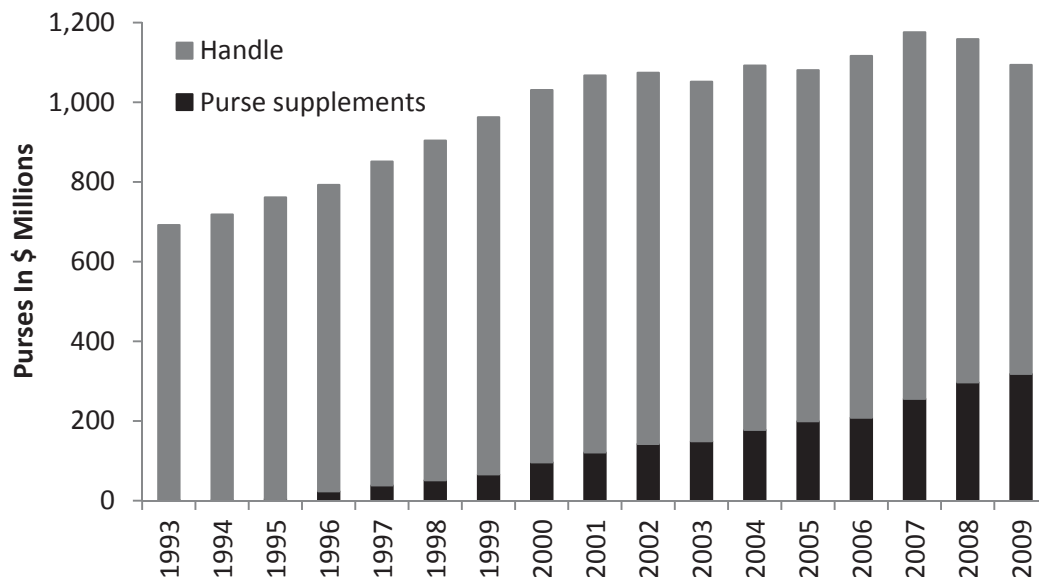
Purses have become increasingly reliant on supplements.

Purses have become increasingly reliant on supplements. For example, in 2000, 10 percent of purses were funded by purse supplements. By 2009, 29 percent of purses came from supplements.

^g Breakage refers to the dollars that remain after payouts are made from a pari-mutuel pool.

^h The states include Arkansas, Delaware, Florida, Indiana, Iowa, Louisiana, Maryland, New Jersey, New Mexico, New York, Oklahoma, and Pennsylvania.

Figure 1.K
Thoroughbred Purses From Handle And Purse Supplements In The US
1993 To 2009



Source: Thoroughbred.

States that increased their purse supplements and breeder's awards increased the earnings potential when a mare's foal is registered or when a racehorse owner wins a race in a particular state. Many of the states that compete with Kentucky are increasing incentives offered to mare owners and racehorse owners. These incentives support the existing Thoroughbred industry in each state and could entice out-of-state Thoroughbred owners to move their horses and spend their money in a particular state.

In Table 1.10, breeder's awards and purses derived from non-pari-mutuel sources for the six selected states are compared to the breeder's awards and purse supplements in Kentucky. In 2000, the difference in the level of incentives offered in Kentucky relative to the selected states was largely due to purse supplements tied to gaming receipts in West Virginia, Indiana, and New York. Beginning in 2002, Louisiana increased its Thoroughbred purse supplements, with funding provided by gaming receipts. From 2005 to 2006, the combined awards and supplements in the selected states declined slightly, mostly because of a reduction in purse supplements in West Virginia. After 2006, the breeder's awards and purse supplements in the selected states increased rapidly again. The increases in 2007 were largely attributable to gaming receipts in Pennsylvania being dedicated to awards and supplements. In 2008, Indiana allowed slots at its two

Thoroughbred tracks, with a portion of the receipts dedicated to purses and breeder's awards. For Kentucky, from 2000 to 2006 the Kentucky Thoroughbred Development Fund was declining in tandem with reductions in live pari-mutuel handle. Once the Kentucky Breeder's Incentive Fund was established, Kentucky's level of incentives increased, but because of substantial increases in the six comparative states, the difference between Kentucky and these six states as a whole continued to grow.

Table 1.10
Thoroughbred Breeders Awards And Purse Supplements In Kentucky And Selected States
2000 To 2009
(\$ Millions)

State	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
Pennsylvania	\$8.8	\$9.5	\$8.8	\$8.3	\$7.9	\$7.3	\$9.5	\$57.8	\$94.7	\$115.3
West Virginia	36.0	48.1	63.7	69.5	74.2	79.5	71.4	66.1	65.2	63.2
Louisiana	3.0	2.0	21.1	30.7	35.7	44.4	44.2	55.2	53.6	56.1
Indiana	8.5	9.3	7.7	7.7	9.0	8.8	8.8	8.5	18.4	28.2
New York	9.0	9.6	9.7	9.8	15.4	17.9	19.5	19.8	19.7	21.0
Florida				0.1	0.1	15.7	16.8	18.9	18.9	18.9
Subtotal	65.3	78.5	111.0	126.0	142.3	173.6	170.1	226.3	270.5	302.6
Kentucky	9.6	9.0	8.7	8.2	7.7	7.3	6.7	19.4	22.0	21.5
Total	\$74.9	\$87.5	\$119.7	\$134.2	\$150.0	\$180.9	\$176.8	\$245.7	\$292.5	\$324.1

Note: Column entries may not add to totals shown due to rounding.

Sources: Thoroughbred Racing Association of North America, state racing associations and commissions, gaming and control boards, auditors' reports, and Kentucky Department of Revenue.

Chapter 2

Kentucky's Programs To Assist The Equine Breeding Industry

Kentucky provides assistance to its horse breeding industry primarily by allocating sales tax revenue collected from stud fees to breeders incentive funds and by allocating revenue from the pari-mutuel tax to various funds including development funds. Kentucky also exempts certain sales related to the equine industry from its sales tax.

The breeders incentive funds available for Thoroughbred, Standardbred, and nonrace breeds are financed from the sales tax collected on stud fees. The state allocates these incentives to breeders based on how their horses perform in races, shows, or contests. Breeders must meet several requirements to qualify for awards from these funds.

Kentucky allocates a portion of its revenue from the pari-mutuel tax to fund equine-related programs.

Kentucky allocates a portion of its revenue from the pari-mutuel tax to fund programs aimed at the equine industry. Statutes require businesses that provide pari-mutuel wagering to allocate a share of the amount wagered at their facilities to these funds. The primary programs tied to the pari-mutuel tax are the development funds, which provide awards to owners of Thoroughbred or Standardbred horses bred in Kentucky. Owners can receive awards under these funds based on the performance of qualifying horses.

This chapter includes an explanation of the funding sources, trends in available amounts of funding, factors that have affected these funds, and how these funds are used. The chapter also discusses how sales and purchases of goods and services related to the equine industry are treated under Kentucky's sales tax.

Kentucky Breeders Incentive Funds

The three breeders incentive funds are the Thoroughbred Breeders Incentive Fund, the Standardbred Breeders Incentive Fund, and the Horse Breeders Incentive Fund.

The three breeders incentive funds, targeting different breeds of horses, are the Thoroughbred Breeders Incentive Fund, the Standardbred Breeders Incentive Fund, and the Horse Breeders Incentive Fund. These funds were established with the enactment of HB 272 in 2005.

Kentucky allocates sales tax revenue on stud fees to these funds, which are administered by the Kentucky Horse Racing Commission.

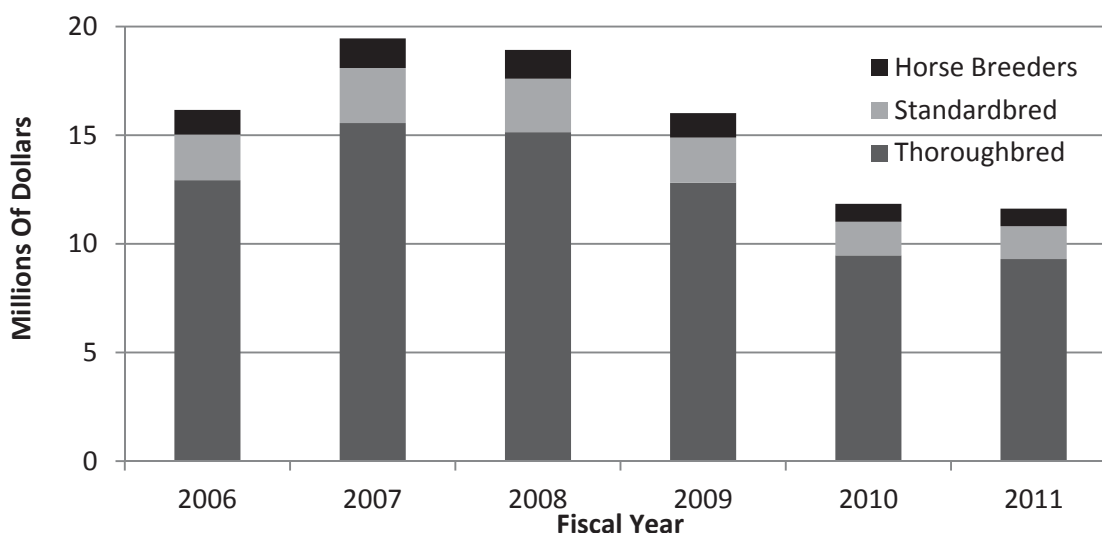
Kentucky charges a 6 percent sales tax on all stud fees in the state. By statute, the sales tax revenue collected from the fees is distributed to the three funds. The Thoroughbred Breeders Incentive Fund receives 80 percent, the Standardbred Breeders Incentive Fund receives 13 percent, and the Horse Breeders Incentive Fund receives 7 percent.

The Kentucky Horse Racing Commission administers the breeders incentive funds and is responsible for promulgating administrative regulations to establish the conditions and criteria for distributing money from each fund.

Funding

Figure 2.A shows the allocation of sales tax revenues collected from stud fees to the three breeders incentive funds. In FY 2006, the breeders incentive funds received \$16.2 million. Allocations to these funds have varied considerably since. The funds increased to \$19.5 million in FY 2007 but declined in each of the next 4 fiscal years.

Figure 2.A
Deposits To Kentucky Breeders Incentive Funds
Fiscal Year 2006 To Fiscal Year 2011



Source: Kentucky. Finance; data for FY 2011 were extracted from eMars by LRC Budget Review staff.

The variability in the annual deposits in the funds is caused by declines in prices for stud fees, declines in the number of mares bred, and changes in breeder operations.

The variability is due to changes in the number of mares bred and the amount paid for stud fees. As yearling sales prices have fallen since 2008, stud fees and the number of mares bred in Kentucky have also fallen, resulting in less sales tax revenue to allocate to these funds. Staff's interviews with horse farm management indicate that changes in breeding operations have also delayed when fees are paid, whether fees are paid, and if so, how much.

Changes in operations include deferment of payments, reduced stud fees, foal sharing, and increased use of free breeding sessions.

Breeders may use arrangements that postpone when the stud fee is paid. Some stud farms now defer payment of the stud fee until the foal is born. In the past, stud fees were typically due by November of the year in which the mare was bred. Under a live foal guarantee, a portion of the fee would not be paid until the foal was born. If the newborn foal was not able to stand and nurse, the amount paid would be refunded. As these arrangements become more prevalent, they delay when the sales tax on the stud fee is collected. Stud farm owners have also indicated they have experienced difficulties collecting stud fees owed to them. To the extent that these fees and the sales tax are eventually paid, this situation delays when the sales tax revenues are collected.

Some arrangements affect the amount of sales tax revenue that is paid on stud fees. For example, in the past several years, some stud farms offered a discount if the stud fee was paid in full by a certain date. Interviews with stud farm managers indicate that some farms offer free or reduced stud fees to mare owners in other states, in exchange for a portion of the breeders award the resulting foal might produce.

In some instances, stud owners enter into foal share agreements under which stud owners provide breeding sessions without cost to the mare owner. No stud fee is paid, so no sales tax is collected. Either the resulting foal is co-owned by the mare owner and the stallion owner, or both parties agree to breed the mare and stallion until two live foals are born—with one foal going to the stud owner and the other going to the mare owner. While foal share arrangements have been in place for years, stud farm managers interviewed by staff indicated its use is increasing.

As part of their compensation for managing a stallion, stud farms receive a limited number of free breeding sessions, which they can either sell or use if they have mares of their own to breed. Two of the stud farm owners staff interviewed had mares of their own and in recent years had used more of their free sessions, rather than sending their mares to a stallion at another stud farm, which would require a stud fee payment.

Declining numbers of mares bred and variability in stud fees will cause future funding levels for the breeders incentive funds to continue to vary, and the potential for growth may be limited.

Kentucky Thoroughbred Breeders Incentive Fund

The Kentucky Thoroughbred Breeders Incentive Fund receives 80 percent of the sales tax generated from stud fees.

The Kentucky Thoroughbred Breeders Incentive Fund, established in KRS 230.800, receives 80 percent of the sales tax revenue generated from stud fees. Table 2.1 shows the fund's annual receipts since FY 2006.

Table 2.1
Deposits To The Kentucky
Thoroughbred Breeders Incentive Fund
Fiscal Year 2006 To Fiscal Year 2011

Fiscal Year	Deposit
2006	\$12,933,787
2007	15,565,451
2008	15,140,333
2009	12,813,442
2010	9,475,867
2011	9,300,333

Source: Kentucky. Finance; LRC
Budget Review staff extracted data
for FY 2011 from eMars.

To qualify for awards from this fund, breeders must register the mare with the Horse Racing Commission, breed the mare to a Kentucky registered stallion, and board the mare in Kentucky until the foal is born.

The Horse Racing Commission developed administrative regulations for distributing the funds in the form of awards to Kentucky Thoroughbred breeders. To qualify, a mare owner must register the mare with the commission, breed the mare to a Thoroughbred stallion that is registered with the commission, and board the mare in Kentucky from the time of breeding until the birth of the foal.

Table 2.2 shows the numbers of stallions and mares that have been registered under the program. Decreases in the number of registered stallions and mares in Kentucky mirror the decline in the United States.

Table 2.2
Stallions And Mares Registered With The
Kentucky Thoroughbred Breeders Incentive Fund
2007 To 2011

Year	Registered Stallions	Registered Mares
2007	337	11,263
2008	324	11,356
2009	325	11,071
2010	303	9,934
2011	271	8,324

Source: Kentucky. Horse.

Breeders receive awards based on foals' winnings.

Once a mare is bred to a Kentucky stallion, the mare owner registers the unborn foal with the program. Registration applications are due by August 1 of the year the mare is bred.^a The mare owner is eligible to receive awards once the foal begins its racing career. Awards are granted to the mare owner based on the foal's winnings in races in Kentucky, in the US, and in certain international races.

The Thoroughbred Breeders Incentive Fund has five components, which target different types of races and provide different levels of awards.

As shown in Table 2.3, the Kentucky Thoroughbred Breeders Incentive Fund program has five components, one of which has two parts. The awards provided under each component vary based on type and location of the race. Awards are based on the performance of the foals but are paid to the breeder of the foal, the owner(s) of the mare. Awards for similar types of races are different depending on whether the race occurs in Kentucky or another state. For example, a breeder could earn an award of 25 percent of the foal's earnings from winning an allowance race in Kentucky but only 10 percent of the winnings for a similar race in another state. Appendix C describes the types of races and the awards provided.

^a Applicants pay a \$60 filing fee, which is used to pay administrative costs. These costs include processing applications, verifying eligibility, and processing awards. The fee generates more than \$500,000 annually.

Table 2.3
Award Structure Of The Thoroughbred Breeding Incentive Fund

Component	Type Of Race	Award Amount	Limit/Description
Kentucky First	Maiden special weight, Allowance, and Stakes	25% of winner's earnings	\$10,000 maximum
National	Maiden special weight and Allowance	10% of winner's earnings	\$10,000 maximum
Kentucky Grade I	Grade I Kentucky Derby and Oaks	\$25,000 \$100,000	
National Grade I	Grade I	\$2,500	
Kentucky Claiming	Claiming	Part 1 \$100,000 Total \$25,000/track	Highest-earning claiming horse at each of 4 tracks
		Part 2 \$100,000 Total 1 st \$50,000 2 nd \$30,000 3 rd \$20,000	Top 3 horses based on Kentucky claiming earnings

Source: Kentucky. Horse; 810 KAR 1:070.

Breeders of winning horses must apply to the commission to receive their awards.

At the end of the calendar year, the commission calculates awards for each component and notifies the breeders of a registered Thoroughbred that has won a race that qualifies under the program. Breeders must then file applications for the awards.^b

If the available funds exceed awards, a limited amount may be held in reserve for providing awards in later years and bonus awards may be paid.

If funds allocated to the Thoroughbred Breeders Incentive Fund exceed the amount needed for awards, the excess funds are placed in a reserve account to be used in years when funding levels are insufficient. Up to 5 percent of the sales tax receipts received in a calendar year may be placed into the reserve account. Once the level of reserves reaches \$5 million, excess funds are no longer added to the account. If money is available after awards and contributions to the reserve fund are made, the commission may provide bonus awards.

In 2010, the commission created an advisory committee to evaluate how awards are made.

Proposed Changes. In fall 2010, the chairman of the Kentucky Horse Racing Commission established an advisory committee to evaluate whether current regulations support the Thoroughbred Breeders Incentive Fund's statutory purpose to support Kentucky's horse industry through awards for breeders of Thoroughbred horses that are bred and foaled in Kentucky. The advisory committee of two members of the commission and seven industry representatives met from October 2010 to May 2011. The committee heard testimony from breeders who received awards, received information from the industry regarding where horses

^b Recipients have 1 year after the end of a calendar year to apply for awards.

foaled in Kentucky race, and researched other states' breeder incentive funds.

The commission recommended decreasing awards for the Kentucky Derby and the Kentucky Oaks, spreading claiming awards across the top 20 horses rather than the top 3, and eliminating differences between awards for races in Kentucky and outside Kentucky.

The commission proposed amending the administrative regulations to reflect the recommendations of the advisory committee. The proposed amendment has gone through the amendment process and will become effective in early November 2011. The recommendations would change awards in three main ways. First, awards for the Kentucky Derby and the Kentucky Oaks would be decreased from \$100,000 to \$50,000. Second, awards for claiming races would be spread over the top 20 claiming horses rather than the top 3. Third, differences between the awards provided for races occurring in Kentucky and outside Kentucky would be eliminated. This was suggested because most Kentucky foals end up racing out of state. The recommendations are described in Appendix C.

Awards. Table 2.4 shows the awards from the Thoroughbred Breeders Incentive Fund. Total annual awards are affected by the number and types of races won by qualified winners and the number of horses eligible for awards.

Since 2006, races in Kentucky accounted for 45 percent of the total amount of awards provided through the fund.

Total awards earned during 2006 were \$12.7 million. In each of the next 2 years, awards exceeded \$15 million, before falling in 2009 and 2010. Since the program began, awards for racing outside the state accounted for 55 percent of total awards.

Table 2.4
Kentucky Thoroughbred Breeders Incentive Fund Awards To Breeders
2006 To 2010

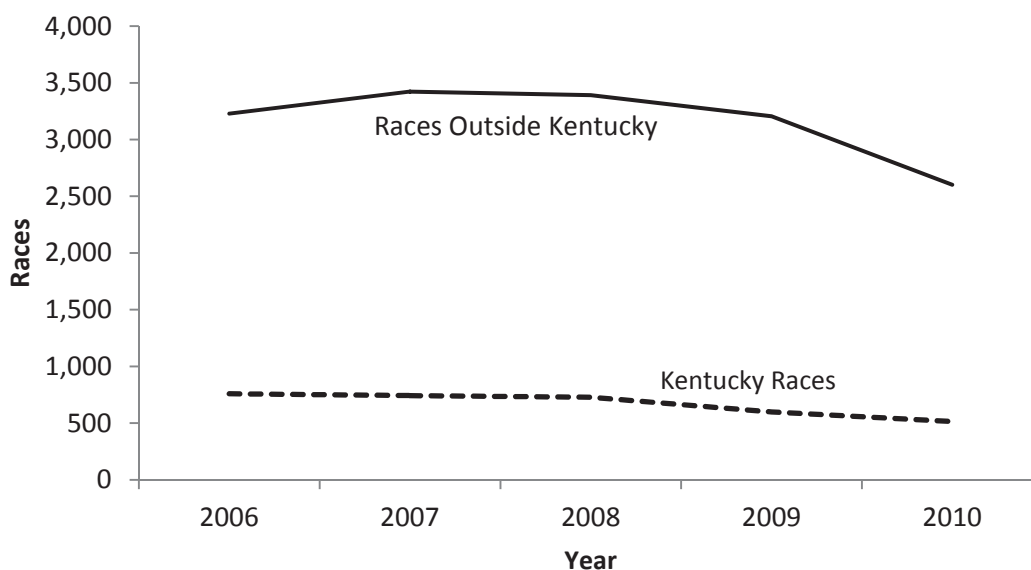
Year	Total	Races In Kentucky		Races Outside Kentucky	
		Awards	Percent Of Total	Awards	Percent Of Total
2006	\$12,654,845	\$6,130,997	48.4%	\$6,523,848	51.6%
2007	15,487,262	6,927,093	44.7	8,560,169	55.3
2008	15,253,911	6,733,924	44.1	8,519,987	55.9
2009	13,409,571	5,712,863	42.6	7,696,708	57.4
2010	10,000,000	4,468,282	44.7	5,531,718	55.3
Total	\$66,805,589	\$29,973,159	44.9%	\$36,832,430	55.1%

Source: Kentucky. Horse.

Since 2006, races in Kentucky accounted for approximately 17 percent of the races resulting in an award.

Figure 2.B shows that the numbers of races resulting in awards from 2006 to 2010 ranged from 3,100 to 4,200 races per year and averaged 3,839 races per year. Kentucky races accounted for 17.4 percent of the races with awards over this period, averaging 669 races per year. Races outside Kentucky accounted for 82.6 percent of the races for which an award was made, averaging 3,170 races per year. Kentucky's percentage of total races resulting in an award has declined.

Figure 2.B
Kentucky Thoroughbred Breeders Incentive Fund, Races Resulting In Awards
2006 To 2010



Source: Kentucky. Horse.

The average award is greater for races in Kentucky than for races outside Kentucky—more than 3 times higher in recent years.

For 2006 to 2010, the average award for races in Kentucky was \$8,696, more than 3 times the average of \$2,324 for races outside Kentucky. The proposed revisions will reduce the level of awards for Kentucky races and will maintain or increase awards for comparable races outside Kentucky.

Kentucky Standardbred Breeders Incentive Fund

The Kentucky Standardbred Incentive Fund receives 13 percent of the sales tax revenue from stud fees. The fund may be used to provide awards to breeders or owners.

Thirteen percent of the sales tax receipts from stud fees is used to promote Kentucky's Standardbred industry. As shown in Table 2.5, annual deposits to this fund exceeded \$2.5 million in Fiscal Year 2007 but have declined in the past 4 fiscal years.

Table 2.5
Deposits To The Kentucky
Standardbred Breeders Incentive Fund
Fiscal Year 2006 To Fiscal Year 2011

Fiscal Year	Deposit
2006	\$2,101,740
2007	2,529,386
2008	2,460,304
2009	2,082,184
2010	1,539,828
2011	1,511,304

Source: Kentucky. Finance; data for FY 2011 were extracted from eMars by LRC Budget Review staff.

KRS 230.802(2)(b) directs that the Kentucky Horse Racing Commission “shall promulgate administrative regulations establishing the conditions and criteria for the distribution of moneys from the fund.”

KRS 230.802 directs the commission to use the fund to provide awards for breeders or owners of Kentucky-bred Standardbred horses. According to subsection (2)(b), “The Kentucky Horse Racing Commission shall promulgate administrative regulations establishing the conditions and criteria for the distribution of moneys from the fund.” Subsection (2)(d) reiterates that the commission “shall disburse moneys in the Kentucky standardbred breeders incentive fund ... under the administrative regulations promulgated pursuant to paragraph (b) of this subsection.”

No administrative regulations exist to direct how money from the Kentucky Standardbred Breeders Incentive Fund is to be disbursed. It is used with the Kentucky Standardbred Development Fund to supplement purses.

No administrative regulations exist to direct how money from the Kentucky Standardbred Breeders Incentive Fund is to be disbursed. Instead, the Kentucky Standardbred Breeders Incentive Fund has been used with the Kentucky Standardbred Development Fund established by KRS 230.770 to supplement purses for the Kentucky Sire Stakes in Kentucky. Although staff did not learn of any problems in how the money from the fund was disbursed, the governing statute requires regulations for how this is to be done.

Recommendation 2.1

Recommendation 2.1

The Kentucky Racing Commission should promulgate administrative regulations establishing the conditions and criteria for the distribution of money from the Kentucky Standardbred Breeders Incentive Fund.

Kentucky Horse Breeders Incentive Fund

The Kentucky Horse Breeders Incentive Fund, which receives 7 percent of the sales tax revenue from stud fees, supports nonrace breeds in Kentucky.

The Kentucky Horse Breeders Incentive Fund receives 7 percent of the sales tax receipts from stud fees each year. It was designed to reward breeders or owners of horses bred and foaled in Kentucky. Table 2.6 shows the annual sales tax receipts deposited into the fund. Funds exceeded more than \$1 million per year through FY 2009 but have since fallen.

Table 2.6
Deposits To The Kentucky
Horse Breeders Incentive Fund
Fiscal Year 2006 To Fiscal Year 2011

Fiscal Year	Deposit
2006	\$1,131,706
2007	1,361,977
2008	1,324,779
2009	1,121,176
2010	829,138
2011	813,779

Source: Kentucky. Finance.

The Horse Breeders Incentive Fund supports nonrace breeds in Kentucky. Texas is the only other state that provides incentive funds for nonrace breeds.

Affiliates for each breed must develop a plan for distributing awards among their members. The Kentucky Horse Racing Commission must approve the plan. Twelve breeds are currently eligible to receive awards from the fund.

To be eligible for awards from the fund, a Kentucky affiliate of each breed that has been certified by the national breed organization must apply to the commission. The affiliate must provide a plan for distributing awards to its members who are breeders or owners of horses bred or foaled in Kentucky. The commission and an advisory committee review the plan. If the plan is approved, the breed affiliate is eligible to receive money from the fund.

Once approved, the breed affiliate's registration and distribution plan is effective for 3 years. The first 3-year registration period was January 1, 2006, to December 31, 2008. The second 3-year registration period is January 1, 2009, to December 31, 2011. Affiliates must file semiannual reports that include a list of the stallions presently breeding horses eligible to participate in the fund and the farm where each stallion stands.

For the current registration period, the commission approved 12 of the 16 Kentucky affiliates that applied for funding. The commission allocates money in the fund to each of the 12 affiliates based on the number of horses 25 years or younger of each breed that reside in Kentucky relative to the total number of horses of all nonrace breeds in Kentucky that have registered and been approved for funding. Individual awards are then made based on each affiliate’s plan. At the end of each calendar year, the affiliates provide the commission with the names of its members who qualify for awards. The commission notifies each award winner, who then must file a claim form in order to receive the award.

Table 2.7 lists the breed affiliates that are currently registered to receive money under the Kentucky Horse Breeders Incentive Fund, the percentage of the fund allocated to each affiliate, and the awards distributed in 2010. For the current registration period, nearly 136,000 horses from the 12 breeds are registered in Kentucky.^c

Table 2.7
Kentucky Horse Breeders Incentive Fund
2010

Registered Kentucky Affiliates	Kentucky Registered Horses	Percent Of Total	Awards Distributed
Kentucky Quarter Horse Association	36,616	26.9%	\$223,412
Kentucky Walking Horse Breeders Incentive Fund	34,923	25.7	213,082
Mountain Horse Breeders Incentive Fund*	13,000	9.6	79,319
Kentucky Saddlebred Owners and Breeders Association	10,925	8.0	66,659
Kentucky Paint Horse Club	10,318	7.6	62,995
Kentucky Arabian and Half Arabian Breeders Alliance	8,086	6.0	49,337
Rocky Mountain Horse Association	7,484	5.5	45,664
Kentucky Miniature Horse Breeders Club	5,726	4.2	34,937
Kentucky Appaloosa Owners Association	4,602	3.4	28,079
South Central Hackney Association	1,505	1.1	9,183
Kentucky Paso Fino Horse Association	1,487	1.1	9,073
Kentucky Morgan Horse Association	1,225	0.9	7,474
Total	135,897	100.0%	\$829,214

*Estimated by Kentucky Horse Racing Commission staff based on registration numbers from the American Gaited Horse Association, the Kentucky Mountain Saddle Horse Association, the Mountain Pleasure Horse Association, and the United Mountain Horse Association.
 Source: Kentucky. Horse.

^c In the initial 3-year registration period, 9 breed affiliates and 115,305 horses were registered.

Equine Programs Funded By The Pari-Mutuel Tax

The majority of Kentucky's pari-mutuel tax is dedicated to funds that help the horse industry. The remainder goes to the general fund.

Kentucky applies a pari-mutuel tax to the amount wagered on live, intertrack, and simulcast races. The tax rate is 3.5 percent for tracks with an average daily live handle of \$1.2 million or more and 1.5 percent for tracks below \$1.2 million.

Thoroughbred tracks pay 3 percent on the amount wagered on intertrack and simulcast races. There is no tax for wagers on intertrack and simulcast races at Standardbred tracks.

Kentucky taxes pari-mutuel wagers at race tracks in the state.^d The majority of revenue collected from this tax is dedicated to programs that assist the equine industry. The remainder goes to the general fund.

Kentucky's pari-mutuel tax applies to wagers placed on live, intertrack, and simulcast races. The tax rate for live races differs depending on each track's average daily live handle—the amount wagered on live races. Tracks with an average daily live handle of \$1.2 million or more pay a tax of 3.5 percent on the amount wagered for live races. Tracks with an average daily live handle of less than \$1.2 million pay a tax of 1.5 percent.

Intertrack wagers are wagers placed at a track on races conducted at another track located in Kentucky. Simulcast wagers are those placed at a track on races conducted at a track located outside Kentucky. Intertrack and simulcast wagers at Thoroughbred tracks are subject to a 3 percent pari-mutuel tax. Intertrack and simulcast wagers at harness tracks are not subject to the pari-mutuel tax (KRS 230.752).^e

KRS 138.510 allocates portions of the pari-mutuel tax to the general fund and four equine-related funds. As shown in Table 2.8, the allocation of tax revenue to these funds differs based on the type of track and the amount of wagering at the tracks.

The Kentucky Thoroughbred Development Fund receives 0.75 percent of the amount wagered on live races at each Thoroughbred track. The Standardbred Development Fund receives 1 percent of the amount wagered on live racing at harness tracks. The Equine Industry Fund receives 0.2 percent of the amount wagered on live races at all tracks. The Higher Education Equine Fund and the Equine Drug Testing Program each receive 0.1 percent of the wagers on live racing.

^d Exempt from the tax are harness races at county fairs and wagers placed at a Kentucky track on days it holds Breeders Cup races.

^e Harness tracks are permitted to use 3 percent of the total amount wagered as follows: 2 percent must be allocated to capital improvements, promotions, advertising, or purses; 0.75 percent must be allocated to purses; and 0.25 percent is dedicated to the Kentucky Standardbred, Quarter Horse, Appaloosa, and Arabian Development Fund.

Table 2.8
Pari-Mutuel Tax Rates On Live Racing As A Percentage Of Amount Wagered

Distribution Of Tax	Average Daily Live Handle		
	\$1.2 Million Or More	Less Than \$1.2 Million	
	Thoroughbred Tracks	Thoroughbred Tracks	Harness Tracks
Development funds*	0.75%	0.75%	1.00%
Equine Industry Fund	0.20	0.20	0.20
Higher Education Equine Fund	0.10	0.10	0.10
Equine Drug Testing	0.10	0.10	0.10
Kentucky general fund	2.35	0.35	0.10
Total tax rate	3.50%	1.50%	1.50%

Note: No Kentucky harness track has an average daily live handle of \$1.2 million or more.

*Kentucky Thoroughbred Development Fund and Standardbred Development Fund.

Source: KRS 138.510.

For tracks with an average daily live handle of \$1.2 million or more, 2.35 percent of wagers on live racing is deposited into the general fund. For tracks with an average daily live handle of less than \$1.2 million, the general fund receives 0.35 percent of live wagers from Thoroughbred tracks and 0.1 percent of live wagers from harness tracks.

The 3 percent pari-mutuel tax on intertrack and simulcast wagers is applied to wagers at Thoroughbred tracks but not at harness tracks. As shown in Table 2.9, the Thoroughbred Development Fund receives 2 percent of intertrack and simulcast wagers. The Equine Industry Fund receives 0.05 percent of intertrack and simulcast wagers. The Higher Education Equine Fund and the Equine Drug Testing Program each receive 0.1 percent of intertrack and simulcast wagers. The general fund receives 0.75 percent of intertrack and simulcast wagers placed at Thoroughbred tracks in the state.

Table 2.9
Distribution Of Pari-Mutuel Tax Rate On Intertrack And Simulcast Wagers At Thoroughbred Tracks

Distribution Of Tax	Percent Of Amount Wagered
Thoroughbred Development Fund	2.00%
Equine Industry Fund	0.05
Higher Education Equine Fund	0.10
Equine Drug Testing Program	0.10
Kentucky general fund	0.75
Total tax rate	3.00%

Source: KRS 138.510.

Revenue collected through the pari-mutuel tax decreased from more than \$18 million in FY 2000 to less than \$11 million in FY 2011, which resulted in lower allocations to the equine funds.

Table 2.10 shows pari-mutuel tax revenue collected and its distribution to the funds.^f Total pari-mutuel taxes have fallen from more than \$18 million in FY 2000 to less than \$11 million in FY 2011. This decline is tied to the decline in pari-mutuel handle from live, intertrack, and simulcast wagering. Allocations to the equine funds have also decreased. From FY 2000 to FY 2011, the state's general fund received 30 to 40 percent of the total pari-mutuel taxes collected.

Table 2.10
Distribution Of Pari-Mutuel Tax Revenue
Fiscal Year 2000 To Fiscal Year 2011

Fiscal Year	Pari-Mutuel Taxes	Kentucky General Fund	Thoroughbred Development Fund	Standardbred Development Fund	Equine Industry Fund	Equine Drug Research	Higher Education Equine Fund
2000	\$18,321,037	\$6,645,098	\$9,552,846	\$334,088	\$575,063	\$606,969	\$606,972
2001	17,335,959	6,182,083	8,979,096	418,428	578,994	588,724	588,634
2002	15,947,368	5,179,952	8,650,050	440,593	545,697	565,642	564,824
2003	16,189,269	5,953,247	8,167,603	427,135	517,373	588,015	535,896
2004	12,830,075	3,629,292	7,668,811	90,426	466,773	487,387	487,387
2005	13,448,435	4,710,111	7,291,319	101,345	469,105	410,068	466,487
2006	13,766,487	5,626,849	6,665,301	109,121	476,831	444,192	444,192
2007	13,847,543	5,489,552	6,789,114	177,674	486,875	452,164	452,164
2008	13,308,919	5,327,540	6,539,512	113,591	460,708	433,784	433,784
2009	12,083,459	4,387,515	6,262,359	310,251	400,309	378,729	344,297
2010*	5,230,141	(82,480)	4,145,106	159,300	359,346	324,435	324,435
2011	10,914,451	4,607,322	5,053,059	310,504	344,465	297,967	297,941

* Historically, the average daily live handle at the state's two largest Thoroughbred tracks exceeded \$1.2 million so the pari-mutuel tax rate paid was 3.5 percent on live wagers. In FY 2009, the tracks paid the tax on live wagers at the higher rate during the year. When the year ended and the average daily live rate for the year was below the \$1.2 million threshold, each track received a refund in FY 2010. The refunds were larger than tracks' deposits to the general fund.

Source: Kentucky Department of Revenue.

^fIn FY 2010, the net amount to the general fund was negative \$82,480. Historically, the average daily live handle at the state's two largest Thoroughbred tracks has exceeded \$1.2 million and the pari-mutuel tax rate paid was 3.5 percent on live wagers. In FY 2009, two tracks paid the tax on live wagers at the higher rate during the year, but once the year ended and the average daily live rate for the year was below the \$1.2 million threshold, each track received a refund in FY 2010. The refunds were larger than deposits to the general fund from wagers at the remaining tracks.

Kentucky Thoroughbred Development Fund

The Kentucky Thoroughbred Development Fund supplements purses for Thoroughbred races won by horses bred in Kentucky.

The Kentucky Thoroughbred Development Fund (KRS 230.400), created during the 1978 Regular Session, was designed to promote and improve Kentucky's Thoroughbred industry. The fund provides purse supplements to the owners of the foal.⁸ The owner of a Thoroughbred foal may qualify if the foal is sired and foaled in Kentucky and wins or places in designated Kentucky races. By providing an incentive to the racehorse's owner, the program tries to encourage owners to buy Kentucky-sired, Kentucky-foaled Thoroughbred horses; to board and breed mares on Kentucky farms to Kentucky stallions; and to race their Kentucky-bred Thoroughbreds at Kentucky tracks. Requiring the horse to be both Kentucky-sired and Kentucky-foaled keeps the mare from becoming eligible for two different state award programs at the same time. Requiring the mares to remain and foal in Kentucky keeps mares in the state longer than if they went back to their home states after being bred to Kentucky stallions, thereby leading to larger economic effects.

Money in the fund comes from a portion of the pari-mutuel tax. Taxes of 0.75 percent on all wagers on live racing and 2 percent on simulcast and intertrack wagers placed at Kentucky Thoroughbred tracks are dedicated to the fund. The fund is used to supplement purses at the Thoroughbred tracks based on each track's contribution to the fund.

The Kentucky Horse Racing Commission and an advisory committee establish the guidelines and regulations for the supplemental purse program. These guidelines and regulations include determining the races eligible for purse supplements, the amount of the supplements, and how payments from the fund will be made.

Purse supplements are available for designated races. To be eligible, a horse must be sired and bred in Kentucky.

Purse supplements are available for designated stakes, handicap, allowance, and nonclaiming maiden races in Kentucky. To be eligible for the supplement, the horse must be registered with the Kentucky Thoroughbred Owners and Breeders Association. Payouts from the purse supplements are 65 percent for the winner, 20 percent for second place, 10 percent for third place, and 5 percent to fourth place in designated races. Since the supplement is added to the purse, the award benefits owners, trainers, and jockeys, since each receives a share of the purse earnings.

⁸ In some cases, the same individuals own the mare and its foal.

If the winner of the race is ineligible for purse supplements, the funds are used for future races.

The races designated to receive purse supplements are not restricted to Kentucky-bred horses. If a noneligible horse wins or places in the top four in a designated race, the purse supplement for that finish position reverts back to the fund and may be used in future designated races.

Table 2.11 shows the total purse supplements offered and paid each year since 2006. The amount offered has fallen over time, and this trend is related to the continual decline in pari-mutuel wagers and pari-mutuel tax receipts.

Table 2.11
Kentucky Thoroughbred Development
Fund Purse Supplements
2006 To 2010

Year	Offered	Paid
2006	\$8,677,600	\$6,811,903
2007	7,165,000	5,740,590
2008	7,989,700	6,044,157
2009	6,745,102	4,957,726
2010	5,838,800	4,660,609
Total	\$36,416,202	\$28,214,985

Source: Kentucky. Horse.

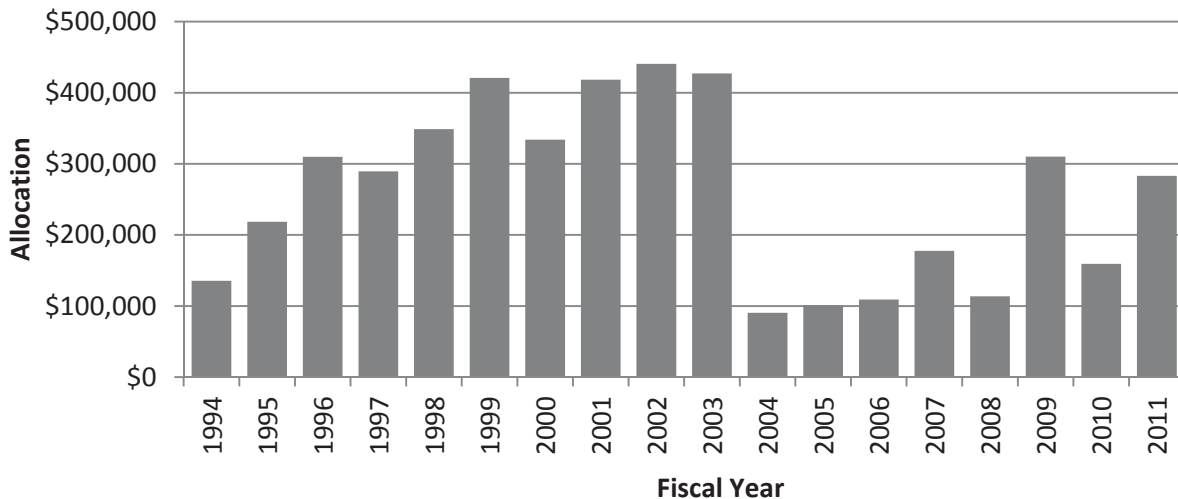
Kentucky Standardbred Development Fund

A portion of the pari-mutuel tax is allocated to the Standardbred Development Fund. Amounts in the fund declined after legislative changes in 2004.

A portion of the annual receipts from the pari-mutuel tax is dedicated to the Kentucky Standardbred Development Fund. This fund receives 1 percent of the wagers on live races at each harness track in the state. Prior to 2004, the fund also received 2 percent of all intertrack and simulcast wagers at each harness track in the state.

Figure 2.C shows allocations to the fund from 1994 to 2011. After the 2004 legislative change exempting harness tracks from the 3 percent tax on simulcast and intertrack wagers, the amount in the Standardbred Development Fund declined significantly.^h

Figure 2.C
Deposits To The Kentucky Standardbred Development Fund
Fiscal Year 1994 To Fiscal Year 2011



Source: Kentucky Department of Revenue.

The Standardbred Development Funds are used along with the Standardbred Breeders Incentive Funds to provide purses for the Kentucky Sire Stakes Program, which is a series of races in Kentucky.

After the enactment of the Standardbred Breeders Incentive Fund, members of the Standardbred industry requested, and the commission agreed, to dedicate both the Standardbred Breeders Incentive Fund and the Standardbred Development Fund to purses for the Kentucky Sire Stakes Program (Kentucky. Horse). The program provides a purse of more than \$2.4 million for certain harness races held in Kentucky.

The Kentucky Sire Stakes is a series of races held annually in Kentucky for qualified 2- and 3-year-old trotting and pacing fillies and colts. Preliminary legs determine the horses eligible for the finals. The final eight races determine the divisional champion of each racing division in the Sire Stakes program. The purse for each preliminary leg is \$30,000, and each divisional final purse is \$250,000.

^h Subsequent legislation (codified as KRS 230.750) required these tracks to allocate 3 percent of the amount wagered to the following: 2 percent for capital improvements, promotions, advertising, or purses; 0.75 percent to overnight purses; and 0.25 percent to the Kentucky Standardbred, Quarter Horse, Appaloosa, and Arabian Development Funds.

To be eligible for the Kentucky Sire Stakes, stallions must be registered with the fund, and the owners of fillies and colts must pay a nomination fee and sustaining payments to remain eligible. To be a participant in a Kentucky Sire Stakes race, the filly or colt must be a product of the mating of a mare with a Kentucky-registered and resident stallion and maintain eligibility for the Kentucky Standardbred Development Fund.

Statistics from the commission indicate 21 stallions were registered with the Standardbred Development Fund in 2011, 19 in 2010, and 27 in 2009. In 2011, nearly 700 yearlings and 2- and 3-year-old fillies and colts were nominated for the program.

Unclaimed Pari-Mutuel Tickets

Unclaimed pari-mutuel tickets at harness races are used to fund purses at harness races occurring at county fairs. Unclaimed pari-mutuel tickets at Thoroughbred races go to the Kentucky Racing Health and Welfare Fund.

Statutes direct that winnings for bets placed at horse races that are not claimed after a period of time be transferred to the Horse Racing Commission; they are used to fund equine-related programs. Funds from the unclaimed tickets at Standardbred tracks are directed to the Kentucky Colt Racing Association to be used for purses at harness races at county fairs.ⁱ Unclaimed winnings at Thoroughbred tracks, which were more than \$2.6 million in 2009, go to the Kentucky Racing Health and Welfare Fund—a nonprofit charitable corporation that provides financial assistance to individuals with limited resources who work at the track.^j

Incentive Programs In Other States

Other states also provide incentive programs to promote their horse breeding industries. The programs are similar to Kentucky's in that they provide awards to breeders and owners of horses bred within the state and the amount of the award is based on the horse's performance. The programs differ in terms of the amounts of awards and which horses qualify for awards.

Other states also provide incentive programs to promote their horse breeding industries. The programs are similar to Kentucky's in that they provide awards to breeders and owners of horses bred within the state and the amount of the award is based on the horse's performance. The programs differ in terms of the amounts of awards and which horses qualify for awards. For example, some awards are provided for races that include only horses that were bred within the state. States also differ in how they fund the programs, but funding sources include tax revenue from pari-

ⁱ In addition to these unclaimed tickets, county fairs also receive 4 percent of the commission from simulcast facilities, approximately \$200,000 per year (KRS 230.380).

^j KRS 230.375 allows the Kentucky Racing Health and Welfare Fund to use 25 percent of annual amounts it receives to fund the Kentucky Race Track Retirement Plan.

mutuel wagering, unclaimed pari-mutuel tickets, and gaming revenue.

Six states that compete with Kentucky for Thoroughbred breeding have incentive programs.

In Chapter 1, staff identified six states that compete with Kentucky for Thoroughbred breeding. The programs for these six states are summarized below.

Florida

The Florida Thoroughbred Breeders and Owners Association offers incentives through its Breeders' Awards Program, which is funded from 0.9955 percent of the handle for all Thoroughbred races in the state (Florida). The program pays 15 percent of the gross purse to any registered Florida-bred horse that finishes first, second, or third. The award is not to exceed \$10,000 for first, \$3,000 for second, and \$2,000 for third. Although Florida has no laws requiring tracks to conduct daily races that are restricted to Florida-bred horses, most tracks run at least three Florida-bred preference races per day. In 2010, the association paid \$5,378,415 in Breeders Awards.

Indiana

The Indiana Horse Racing Commission offers incentives to promote the state's horse breeding industry (Indiana). Indiana's Breeder Award is paid to the breeder of a registered Indiana-bred that wins any race in the state. The amount awarded for nonrestricted races is 25 percent of the winner's share of the purse; the award amount is 20 percent of the gross purse for restricted races. Although there are no laws that require racetracks to offer restricted races, most tracks run two to four races per day that are restricted to Indiana-bred horses. The latest figures available show that the Indiana Horse Racing Commission paid \$1,703,133 in Breeder Awards in 2009, which was 17 percent of total allocations for thoroughbred incentives.

Other awards offered by the commission include stallion owner awards, out-of-state awards, and various purse supplements. The Indiana Horse Racing Commission distributed \$9,811,375 in Thoroughbred awards in 2009.

Louisiana

The Louisiana Racing Commission provides monetary incentives to horse breeders for breeding horses within the state (Louisiana. Gaming. *Annual, Revenue.*) Under the Louisiana Breeder's Fund,

which was established in 1969, breeders of horses in Louisiana are eligible to receive monetary awards of up to 20 percent of race earnings if their horse finishes in the top three of any race in Louisiana. In recent years, the fund allocated approximately \$10 million annually to horse breeders. Fund revenues come from pari-mutuel wagers, off-track betting parlors, and casinos.

Monetary awards are also provided to Louisiana horse breeders if their horse wins, places, or shows in a race outside of Louisiana. Known as the Worldwide Breeder's Fund, this fund awards up to a total of \$400,000 each year to horse breeders. According to the Louisiana Racing Commission, awards are proportioned according to a horse's race earnings and typically average 15 percent to 16 percent of race earnings.

New York

The New York Thoroughbred Breeding and Development Fund Corporations administer awards designed to promote New York's horse industry (New York). They are financed in part by a small percentage of the total money wagered on Thoroughbred racing in New York state and video lottery terminals at the Finger Lakes Racing Casino and Racetrack. One of the awards is the Breeders Award. If a winning horse is sired by a registered New York stallion and foaled in the state, the breeder receives an award of 20 percent of the winnings for a first-place finish or 10 percent for a second- or third-place finish in any race run in New York. If the stallion was not registered in New York, but the horse was foaled in New York, the award is 10 percent for first place and 5 percent for second or third place. Although there is no law requiring racetracks to have races restricted solely to New York-bred horses, most tracks run several each day. In 2010, the fund paid \$6,646,168 in Breeders Awards.

The fund also pays awards to the owner of New York-bred horses and to the owner of the stallion that sired the winning New York-bred horse. In 2010, the fund paid \$1,559,369 in stallion awards and \$859,622 in owner awards.

Pennsylvania

The Pennsylvania Breeding Fund Program offers incentives for the state's Thoroughbred industry (Pennsylvania. Gaming; Pennsylvania. Dept. of Agriculture. *Report*, State). The fund is financed through a percentage of the state's Thoroughbred pari-mutuel handle and slot machine revenues. The Breeders Award is

paid in an amount equal to 30 percent of the purse for every registered Pennsylvania-bred horse that was sired by a registered Pennsylvania stallion and that finishes first, second, or third in any race run in Pennsylvania. If the winning horse was sired by a nonregistered stallion, the fund pays an amount equal to 20 percent of the purse. Although there is no law requiring racetracks to conduct daily races that are restricted to Pennsylvania-bred horses, most tracks offer one or two such races each day. In 2010, the Pennsylvania Breeding Fund Program paid \$6,154,244 in breeder awards.

The fund also pays an award equal to 10 percent of the purse to the owner of Pennsylvania-bred horses and to the owner of the stallion that sired the winning Pennsylvania-bred horse. In addition, the fund provides purse supplements for Pennsylvania-bred stakes races and various other races throughout the year. In total, the Pennsylvania Breeding Fund Program paid \$16,079,611 in 2010.

West Virginia

The West Virginia Racing Commission offers incentives through its Thoroughbred Development Fund, which is supported by a portion of the state's slot machine revenue (Brisbin; West Virginia. Legislative, Racing). Sixty percent of the fund is reserved for bonuses paid to the breeders of accredited Thoroughbred horses that earn a purse at West Virginia racetracks. The bonuses are distributed at the end of the year in an amount according to the ratio of purses earned by an accredited horse to the total amount earned in the participating races by all accredited racehorses for that year, not to exceed \$100,000. The Thoroughbred Development Fund is also used to provide bonus awards to the owner of accredited Thoroughbreds (25 percent) that earn a purse and to the owner of the stallions that sired those winners (15 percent). West Virginia law requires racetracks to hold two races each day that are restricted solely to West Virginia-bred horses. In 2010, the commission paid out approximately \$8.1 million in Thoroughbred Development Funds.

The commission also provides incentives through its Supplemental Purse Program. This program was funded primarily through unredeemed pari-mutuel tickets but recently began receiving a small portion of the state's lottery revenue. Awards are given to any West Virginia-bred horse that finishes first at a racetrack in the state, and the program pays 10 percent of the winner's purse each to the owner and breeder of the racehorse and the owner of the sire. In previous years, the program had insufficient funds to distribute

awards. Officials with the West Virginia Racing Commission said they expect to begin making awards in 2013 and estimated that they would pay approximately \$1.6 million.

Sales Tax Exemptions Related To Kentucky's Equine Industry

Kentucky provides some sales tax exemptions for transactions related to the horse industry.

States may assist a specific industry by exempting from the sales tax the sales of certain goods and services used by or produced by the industry. By exempting the purchase of goods and services that an industry needs, the state lowers the cost of doing business for that industry. By exempting the goods and services the industry produces, the state can lower prices of the industry's output and possibly increase sales. Kentucky sales tax is applied to a number of sales transactions related to the horse industry but does exempt certain transactions.

The sales tax is applied to stud fees. However, if stallion services are traded, the transaction would not be taxed. The sale of horses is taxed, but some types of horse sales are not. Horse sales not taxed include purchases for breeding purposes, sales across state borders, sale for resale, sales of horses less than 2 years of age if sold to someone who is not a resident of Kentucky, and sales of farm work stock.^k Fees for boarding and training horses are also exempt from the sales tax.

Six inputs are exempt for certain types of farms but are taxed for equine.

Kentucky's exemptions for the equine industry differ from the exemptions provided for other types of agricultural production. Table 2.12 highlights differences in how agricultural goods are treated under the sales tax. Six are exempt for certain types of agricultural production but are taxed for equine. For example, farm machinery and repair parts would be taxed if purchased by a horse farm but not if purchased for use in crop, livestock, or poultry production.

^k Farm work stock is not statutorily defined; however, the term would commonly include draft horses, mules, and donkeys.

Table 2.12
Kentucky Sales Tax Exemptions For
Equine, Crop, Livestock, Poultry, And Alternative Agriculture Production

Type Of Sales	Equine	Crop	Livestock And Poultry	Alternative Agriculture
Sales for resale	✓	✓	✓	✓
Interstate commerce sales	✓	✓	✓	✓
Breeding stock sales	✓		✓	✓
Baling twine and wire	✓	✓	✓	✓
Water	✓	✓	✓	✓
Seed and fertilizer		✓	✓	✓
Farm chemicals		✓	✓	✓
Feed and feed additives			✓	✓
Farm machinery and repair parts		✓	✓	✓
Fuels		✓	✓	✓
On-farm facilities		✓	✓	✓

Note: Alternative agriculture farms include aquaculture, buffalos, ratites, llamas, and cervidae.
 Source: Kentucky Revised Statutes.

Table 2.13 compares how Kentucky and eight other states apply sales tax to different types of sales and fees related to the equine industry. The states shown are those that Kentucky competes with based on the number of Thoroughbred mares bred in each state. Based on these five categories of sales and services relating to horse farms, it appears the application of the sales tax in Kentucky is similar to the sales tax treatment in these eight comparative states.

Table 2.13
Equine Industry Fees And Sales Exempted From Sales Tax By State

State (Exemptions)	Sales Tax Rate	Stud Fees	Boarding	Horses Claimed	Breeding Stock (Stallions/Mares)	Nonbreeding Horses
California (3)	7.25%	✓	✓		✓	
Florida (4)	6.00	✓	✓		✓	✓
Illinois (5)	6.25	✓	✓	*	✓	✓
Indiana (2)	7.00	✓	✓			
Kentucky (2)	6.00		✓		✓	
Louisiana (5)	4.00	✓	✓	✓	✓	✓
Maryland (3)	6.00	✓	✓		✓	
New York (2)	4.00	✓			✓	
Pennsylvania (5)	6.00	✓	✓	✓	✓	✓

*Exempted if sale is made by the breeder.
 Source: Staff analysis of states' statutes.

Of eight states with which Kentucky competes based on the number of Thoroughbred mares bred, none apply the sales tax to stud fees. Kentucky does but allocates the tax revenue to breeders incentive funds.

Kentucky is the only state of those reviewed that taxes stud fees, but the sales tax receipts from these fees provide assistance to the equine industry through the breeder incentive funds. In New York, the sales tax is applied to boarding fees, but all the remaining states exempt boarding fees from the sales tax. Pennsylvania began exempting the sale of horses claimed at its racetracks in 1996. Louisiana began exempting claiming horse sales in 2007. The remaining states apply the sales tax to the sales of claiming horses. With the exception of Indiana, each state exempts the sales of breeding stock. For sales of nonbreeding stock, one-half of the states exempt these sales but limit the exemption to sales made by the breeder or sales relating to racehorses.

Table 2.14 summarizes whether certain inputs purchased by horse farms are exempt from the sales tax. Among these states, only New York provides a sales tax exemption for building materials for horse farms, but the exemption is limited to commercial operations. Purchases of machinery and equipment are exempt in four states and in Maryland and Pennsylvania if the farm is a commercial breeding operation.

Table 2.14
Sales Tax Exemptions For Equine Industry Inputs By State

State (Exemptions)	Building Materials	Farm Machinery And Equipment	Feed	Horse Supplies	Services	General Farm Inputs
California (3)		✓	✓		✓	
Florida (4)		✓	✓		✓	✓
Illinois (3)		✓	*		✓	✓
Indiana (1)					✓	
Kentucky (1)					✓	
Louisiana (3)			✓		✓	✓
Maryland (5)		✓	✓	✓	✓	✓
New York (6)	✓	✓	✓	✓	✓	✓
Pennsylvania (5)		✓	✓	✓	✓	✓

Note: Services include veterinarian, dental, accounting, advertising, bloodstock, and marketing. General farm inputs include fuel, oil, seed, fertilizer, and chemicals. Sales tax receipts for horse feed sales are allocated to equine research and education.

*Sales tax receipts for horse feed are allocated for equine research and education.

Source: Staff analysis of states' statutes.

Purchases of feed for horses are exempt from the sales tax in six of the nine states. Florida exempts all horse feed sold; five states exempt these sales if made to a commercial operation or breeder.

Six of the nine states apply the sales tax to horse supplies. Three allow an exemption if the horse supplies are purchased by commercial operations or operations that breed horses.

None of the states reviewed apply the sales tax to services such as veterinarian, dental, accounting, advertising, bloodstock, and marketing services used by horse operations. This is consistent with states typically not collecting sales taxes on services in general.

General farm expenses such as fuel, oil, seed, fertilizer, and chemicals are exempt from the sales tax in six of the other states. Of the six, Maryland, New York, and Pennsylvania limit the exemption to breeding or commercial operations.

Comparing Kentucky to the other eight states, Kentucky's application of the sales tax to building materials, horse supplies, and services used by horse farms is similar to most of the other states. Kentucky and two other states apply the sales tax to farm machinery and equipment purchases made by horse farms. Kentucky and Indiana are the only states that tax horse feed in which the proceeds are allocated to the state's general fund. Kentucky and two other states apply the sales tax to general farm inputs used on commercial horse farms. Kentucky and Indiana are the only states that tax all inputs except services. New York exempts all inputs, and Pennsylvania exempts all inputs except building materials.

Chapter 3

Economic Contribution of Kentucky's Thoroughbred Breeding Industry

Kentucky's Thoroughbred breeding industry contributes to the state's economy directly through the workers it employs and indirectly through the purchase of inputs from other businesses.

The committee directed staff to estimate how the Thoroughbred breeding industry contributes to the state's economy. The industry contributes to the state's economy directly by employing workers. The industry contributes to the state's economy indirectly as Thoroughbred breeding farms purchase inputs such as feed, hay, and bedding needed to support their operations from other businesses located within the state. Thoroughbred farms purchase services from equine-related professionals such as veterinarians and farriers and other professional services such as accountants and attorneys. Through what is sometimes referred to as the inducted effect, the industry also affects the state's economy indirectly when its employees and the employees of the supporting businesses spend their earnings on goods and services produced within the state.

Estimating Total Economic Contribution

Economic contributions are typically measured by spending, employment, and earnings.

The economic contribution of an industry such as Thoroughbred breeding is typically measured in terms of sales, employment, and earnings. Sales refer to the value of the goods and services produced and sold, employment refers to full-time and part-time jobs, and earnings are the wages and salaries paid to workers.

Economic multipliers measure the degree to which economic activity in one industry affects economic activity in other industries located within the state.

An industry's total economic contribution can be measured by estimating the amount of spending or employment that occurs directly within the industry and applying economic multipliers to these estimates. Economic multipliers measure the degree to which spending, employment, or earning in one industry of an economy affects the spending, employment, and earnings within the total economy.

For example, a multiplier with the value 1.5 measuring the relationship between spending in one industry and spending in the total state economy would indicate that for every dollar spent by an industry an additional 50 cents is spent within the economy.

The values of multipliers are determined partially by how much of the spending is for goods and services produced within the state. For example, to produce wooden fencing material for a farm, one

firm had to harvest timber. This firm would then sell the timber to a second firm that cuts the timber to make fence materials. If both firms are located in Kentucky, multipliers for the state would be larger than if one or both are located in another state. If the timber company harvests the timber in another state, the economic effects on spending, employment, and earnings would accrue in the other state. To the extent that spending occurs on items that are produced in other states the multipliers will be lower. Multipliers that measure employment and earnings are also affected by how much labor is required to produce the goods and services and the wages paid to the workers producing the goods and services.

For this analysis, staff used RIMS II economic multipliers, which were developed by the US Bureau of Economic Analysis.

Economic multipliers are estimated based on historical data on the state's economy. For this analysis, staff used RIMS II economic multipliers, which were developed by the US Bureau of Economic Analysis (US. Dept.).^a

Staff estimated that the Thoroughbred breeding industry spent approximately \$912 million in 2010.

To estimate the economic effects associated with Thoroughbred breeding, staff needed information on the amount of spending in this industry. The survey results indicate that Thoroughbred breeding farms had an average of 66 horses per farm and spent \$21,690 per horse in 2010. Applying these averages to the 637 Thoroughbred breeding farms that were sent a survey indicates that there are 42,042 horses on these farms with total annual expenditures of approximately \$912 million.^b

The estimates presented do not represent the economic loss that would occur if the industry left the state.

The estimates presented in this chapter do not reflect the economic loss Kentucky would experience if the Thoroughbred breeding industry were to exit the state. If breeding farms exited the state, they would leave resources, primarily land, which could be used to produce something other than Thoroughbreds. The farmland could be used to raise crops, or cattle or could be developed. These alternative uses for the resources would also contribute to the economy, offsetting at least a portion of the losses from the

^a There is no multiplier specifically for Thoroughbred breeding farms, which may have different spending patterns from other horse farms. The most detailed multiplier is based on economic activity for "other animal production," which includes Thoroughbreds but also other horses, llamas, alpacas, buffalo, deer, and worms. Because most of the spending within this industry in Kentucky comes from horse farms, any potential bias may not be large.

^b Farms that responded to the survey could differ from those that did not respond in terms of the number of horses or the expenditures per horse, which could bias the estimate of total expenditures. To check for potential bias, staff compared the estimates of daily board rates and other maintenance costs from the survey to estimates from a 2001 study by Thalheimer and Lawrence. The daily board rates and other maintenance costs from the 2011 survey were higher than those reported in 2001, but the differences were not large, especially considering the time between estimates.

breeding farms. The economic impact of the Thoroughbred breeding industry is the difference in spending, employment, and earnings with Thoroughbred breeding and the alternative use of the resources that would remain.

Estimated Contribution To Spending In Kentucky

The estimated \$912 million spent directly by the Thoroughbred breeding industry resulted in total estimated spending in Kentucky of \$1,584.6 million.

Table 3.1 shows the direct, indirect, and total spending associated with Kentucky's Thoroughbred breeding industry. Staff estimated that Kentucky's Thoroughbred farms had total expenditures of \$912 million in 2010. The output multiplier from RIMS II was 1.7376, indicating that for each \$1 spent in this industry approximately \$0.74 is spent in other industries within Kentucky's economy.^c This suggests that the \$912 million in spending by the Thoroughbred breeding industry results in an additional \$672.7 million in spending in other areas of the state's economy. This represents the indirect effect on spending. The estimated total amount of spending resulting from the Thoroughbred breeding industry is \$1,584.6 million.

This spending occurred across several industries including construction and manufacturing.

Table 3.2 shows how the total spending that is associated with Thoroughbred breeding is distributed across different industries of Kentucky's economy. More than 41 percent of the indirect spending is in the agricultural sector, which includes other farms and farm supply firms. Thoroughbred farms' investments in barns, buildings, and other facilities lead to additional spending in the construction and manufacturing sectors, which account for nearly 22.4 percent of the indirect spending. Finance and insurance, real estate, and professional and managerial services account for 14 percent of the indirect spending.

^c Motor vehicle, body, trailer, and parts manufacturing is the only industry in Kentucky with a higher multiplier in the RIMS II model.

Table 3.1
Estimated Total Kentucky Spending Associated With
The Thoroughbred Breeding Industry In 2010

Output	Percent	Spending (\$ Millions)
Direct (Thoroughbred breeding industry)	58%	\$911.9
Indirect (other industries)	42	672.7
Total	100%	\$1,584.6

Note: The output multiplier (Total Output/Direct Output) is 1.7376.

Source: Staff analysis using RIMS II.

Table 3.2
Distribution Of Estimated Indirect Spending By Industry In 2010

Industry	Spending (\$ Millions)	Percent Of Indirect Spending
Agriculture	\$278.9	41.4%
Construction and manufacturing	150.5	22.4
Finance and insurance, real estate, professional services, managerial services	95.1	14.1
Wholesale and retail trade	57.0	8.5
Transportation	42.8	6.4
Other industries	48.4	7.2
Total	\$672.7	100.0%

Source: Staff Analysis using RIMS II.

Estimated Contribution To Kentucky Employment

Data from RIMS II indicate that for every 100 jobs in the Thoroughbred breeding industry, there are 64 jobs in other industries that help support the Thoroughbred breeding industry.

Staff estimate that there were approximately 10,800 jobs within the Thoroughbred breeding industry in 2010.

Total employment associated with the industry, including indirect employment, is estimated to be 17,657 jobs.

The employment multiplier from RIMS II for the Thoroughbred industry is 1.635. This indicates that for each 100 jobs in the Thoroughbred breeding industry, there are approximately 64 full- and part-time jobs in other industries within Kentucky that help support the breeding industry.

Table 3.3 shows the direct, indirect, and total employment associated with Kentucky's Thoroughbred breeding industry. Based on the survey, staff estimated there were 10,797 jobs directly associated with Kentucky's Thoroughbred breeding industry in 2010.

By applying the RIMS II employment multiplier to the number of direct jobs, staff estimated that there were 17,657 jobs related to the Thoroughbred breeding industry in 2010. This included 6,860 jobs in other industries that provide goods and services to the Thoroughbred breeding industry.

Table 3.4 shows how these jobs are distributed by industry. Nearly 48 percent of the jobs linked to Thoroughbred breeding are in the agricultural sector. Jobs in the finance and insurance, real estate, professional services, and managerial services category account for nearly 20 percent of the jobs related to the Thoroughbred breeding industry. A number of construction and manufacturing jobs and equine transportation jobs are tied to spending on Thoroughbred breeding due to the capital investment and movement of horses. Spending by those who work in the Thoroughbred breeding industry and the supporting sectors also helps support employment in the wholesale and retail trade sectors.

Table 3.3
Estimated Kentucky Employment Associated With
The Thoroughbred Breeding Industry In 2010

Employment	Jobs	Percent
Direct	10,797	61%
Indirect	6,860	39
Total	17,657	100%

Note: The multiplier (total jobs/direct jobs) is 1.635.

Source: Staff analysis using RIMS II.

Table 3.4
Distribution Of Estimated Indirect Employment In 2010 By Industry

Industry	Jobs	Percent
Agriculture	3,302	48.1%
Finance and insurance, real estate, professional services, managerial services	1,377	20.1
Construction and manufacturing	653	9.5
Wholesale and retail trade	583	8.5
Transportation	406	5.9
Other	539	7.8
Total	6,860	100.0%

Note: Percentages do not sum to 100.0 due to rounding.

Source: Staff analysis using RIMS II.

Estimated Contribution To Kentucky Earnings

Total annual earnings associated with the industry for 2010 was estimated to be \$352.7 million.

As shown in Table 3.5, average earnings were \$15,549 per job within the Thoroughbred breeding industry and \$26,942 for indirect jobs in 2010.^d Applying these averages to the employment estimates indicates that direct earnings totaled \$167.9 million and indirect earnings totaled \$184.8 million in 2010. For every \$1 in earnings paid within the Thoroughbred breeding industry, another \$1.1 in earnings was paid in other industries within the economy. The total earnings associated with the Thoroughbred industry were estimated to be \$352.7 million in 2010.

Table 3.5
Estimated Kentucky Annual Earnings Associated With
The Thoroughbred Breeding Industry In 2010

Earnings	Earnings (\$ Millions)	Percent	Average Earnings Per Job
Direct	\$167.9	47.6%	\$15,549
Indirect	184.8	52.4	26,942
Total	\$352.7	100.0%	
Overall average			\$19,975

Note: The multiplier (total earnings/direct earnings) is 2.1.

Source: Staff analysis using RIMS II.

Table 3.6 shows how the total earnings were distributed by industry. Distribution by sector followed the same pattern as for employment.

Table 3.6
Distribution Of Estimated Indirect Earnings In 2010 By Industry

Industry	Percent	Earnings (\$ Millions)	Earnings Per Job
Agriculture	34.3%	\$63.5	\$19,227
Finance and insurance, real estate, professional services, managerial services	18.0	33.2	24,073
Construction and manufacturing	15.6	28.9	44,269
Wholesale and retail trade	13.0	24.0	41,166
Transportation	9.3	17.3	42,556
Other	9.7	17.9	33,209
Total	100.0%	\$184.8	
Average earnings per indirect job			\$26,942

Note: Percentages do not sum to 100.0 due to rounding.

Source: Staff analysis using RIMS II.

^d Earnings are lower than personal income, which includes income from sources other than employment such as dividends, interest, and government payments.

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Appendix A

How This Study Was Conducted

In completing this study, staff interviewed staff of the Kentucky Horse Racing Commission, representatives of the Kentucky Thoroughbred Owners and Breeders Association, and owners and managers of Kentucky Thoroughbred horse farms. Staff reviewed statutes, administrative regulations, and meeting minutes to understand how Kentucky provides assistance to its horse breeding industry. Staff reviewed documents from other states to determine how these states promote their breeding industries.

Staff also conducted a survey of Kentucky's Thoroughbred operations. These results were applied to an economic model of the state's economy to estimate how the Thoroughbred breeding activity affects other sectors of the state's economy.

Appendix B

Kentucky Thoroughbred Industry Survey

Kentucky Thoroughbred operations were surveyed by mail in August and September 2011. Respondents were instructed that responses should pertain only to operations located in Kentucky. For Thoroughbred farms with more than one location in Kentucky, respondents were instructed to submit one response to cover all the locations.

The questions and summarized responses are below. Most questions were open ended. LRC staff compiled responses to these questions into categories. Totals may not add to the numbers shown in the tables due to rounding.

Type and Size of Operation

1. Which of the following categories would best describe your equine operation in Kentucky?
(check only one response)

Category	% Of Total	
	Farms	Farms
Horse breeding operation (stud or broodmare farm, or an operation with both enterprises)	59	39.3%
Horse boarding operation (an operation that derives the majority of its gross income by providing boarding services to clients)	34	22.7
Diversified horse operation (operation with 3 or more divisions such as stud, broodmare, boarding, weanling and yearling, sales preparation, or training)	41	27.3
Other type of equine operation	16	10.7
Total	150	100.0%

2. In the box below, indicate the total acres in your Kentucky operation as of January 1, 2011. (Include the number of acres owned and the number of acres rented from others. Do not include land that is rented to others.)

[Open-response question: LRC staff compiled the responses into categories.]

Acres	Farms	% Of Total
		Farms
100 or fewer	54	37.5%
101 to 250	37	25.7
251 to 500	27	18.8
501 to 1,000	16	11.1
More than 1,000	10	6.9
Total	144	100.0%

Equine Inventory

1. In the table below, indicate the number of equines that were located on your Kentucky equine operation as of January 1, 2011, that you fully owned, partially owned, or boarded for others.

Category	Horses	% Of Total
		Horses
Full ownership	3,972	46.9%
Partial ownership	1,104	13.0
Boarded for others	3,396	40.1
Total	8,472	100.0%

Note: 150 respondents.

2. In the table below, indicate the number of breeding and nonbreeding stock located on your Kentucky equine operation, regardless of ownership, as of January 1, 2011.

		% Of Total	
		Horses	Horses
Breeding stock	Stallions	114	1.3%
	Broodmares	4,215	48.5
Total breeding stock		4,329	
Nonbreeding stock	Foals and weanlings	1,206	13.9
	Yearlings	2,138	24.6
	2-years old or older	1,024	11.8
Total nonbreeding stock		4,368	
Total stock		8,697	100.0%

3. For calendar year 2010, estimate the average daily number of equines located at this operation during the breeding season.

[Open-response question: LRC staff compiled the responses into categories.]

Average Daily Number Of Horses	Farms	% Of Total Farms	% Of Total Horses
10 or fewer	30	22.4%	2.2%
11 to 20	21	15.7	3.8
21 to 30	14	10.5	4.2
31 to 50	21	15.7	11.1
51 to 100	26	19.4	23.5
101 to 200	13	9.7	21.2
More than 200	9	6.7	34.0
Total	134	100.0%	100.0%

4. How many mares were bred at this operation during calendar year 2010?

[Open-response question. LRC staff compiled the responses into categories.]

Mares Bred	Farms	% Of Total Farms	% Of Total Mares Bred
10 or fewer	44	35.2%	2.3%
11 to 30	31	24.8	6.2
31 to 100	38	30.4	22.1
101 to 800	7	5.6	10.3
More than 800	5	4.0	59.1
Total	125	100.0%	100.0%

5. How many mares foaled at this operation during calendar year 2010?

[Open-response question: LRC staff compiled the responses into categories.]

Mares That Foaled	Farms	% Of Total Farms	% Of Total Mares That Foaled
5 or fewer	35	29.2%	3.4%
6 to 15	26	21.7	8.2
16 to 30	24	20.0	18.3
31 to 50	20	16.7	26.0
More than 50	15	12.5	44.2
Total	120	100.0%	100.0%

Expenditures and Employees

1. What was the amount of gross expenditures for your Kentucky equine operation in calendar year 2010?

[Open-response question: LRC staff compiled the responses into categories.]

Gross Expenditures	Farms	% Of Total Farms	% Of Total Expenditures
\$100,000 or less	22	20.0%	0.6%
\$100,001 to \$250,000	23	20.9	2.2
\$250,001 to \$500,000	16	14.6	3.2
\$500,001 to \$ 1,000,000	24	21.8	10.6
\$1,000,001 to \$2,000,000	9	8.2	7.0
More than \$2,000,000	16	14.6	76.4
Total	110	100.0%	100.0%

2. Indicate the number of employees dedicated to your Kentucky equine operation during calendar year 2010.

A. Total number of full-time, year-round employees

[Open-response question: LRC staff compiled the responses into categories.]

Full-Time Employees	Farms	% Of Total Farms	% Of Total Full-Time Employees
0	10	7.7%	0.0%
1 to 5	71	54.6	10.3
6 to 15	26	20.0	15.0
16 to 30	13	10.0	17.3
31 to 100	7	5.4	25.8
More than 100	3	2.3	31.6
Total	130	100.0%	100.0%

B. Total number of part-time or seasonal employees

[Open-response question: LRC staff compiled the responses into categories.]

Part-Time Or Seasonal Employees	Farms	% Of Total Farms	% Of Total Part-Time Or Seasonal Employees
0	20	17.1%	0.0%
1	32	27.4	6.6
2	27	23.1	11.1
3 to 5	23	19.7	16.9
More than 5	15	12.8	65.4
Total	117	100.0%	100.0%

B1. Average number of weeks worked for part-time or seasonal employees

[Open-response question: LRC staff compiled the responses into categories.]

Part-Time Or Seasonal Employees	Farms	% Of Total Farms
5 or fewer	7	7.8%
6 to 10	14	15.6
11 to 20	32	35.6
21 to 40	24	26.7
More than 40	13	14.5
Total	90	100.0%

B2. Average number of hours worked each week for part-time or seasonal employees

[Open-response question: LRC staff compiled the responses into categories.]

Part-Time Or Seasonal Employees	Farms	% Of Total Farms
Fewer than 10	9	9.9%
10 to 19	9	9.9
20 to 34	21	23.1
35 to 44	24	26.4
45 or more	28	30.8
Total	91	100.0%

Income

1. What was the gross income of your Kentucky equine operation in calendar year 2010?

[Open-response question: LRC staff compiled the responses into categories.]

Gross Income	Farms	% Of Total Farms	% Of Total Income
\$100,000 or less	32	27.1%	0.7%
\$100,001 to \$300,000	25	21.2	2.7
\$300,001 to \$1,000,000	37	31.5	12.7
\$1,000,001 to \$3,000,000	12	10.2	12.3
\$3,000,001 to \$10,000,000	7	6.0	15.4
More than \$10,000,000	5	4.3	56.2
Total	118	100.0%	100.0%

2. In the table below, estimate the 2010 income of your Kentucky equine operation for each category.

Category	Income	% Of Total
Equine sales	\$44,003,450	24.0%
Stud fees	55,565,530	30.4
Management fees and commissions	4,396,836	2.4
Boarding fees	41,617,940	22.7
Sales preparation fees	1,633,060	0.9
Training fees	4,413,813	2.4
Other*	31,410,510	17.2
Total	\$183,041,139	100.0%

Note: 118 respondents.

* The "Other" category was not listed on the questionnaire. For each respondent, the value for "Other" was created by subtracting the total of the six categories in question 2 from the response for gross income in question 1.

3. How many weanlings, yearlings, and two year-old equines, owned in full or in partnership by this operation, were sold in calendar year 2010?

[Open-response question: LRC staff compiled the responses into categories.]

Horses Sold	Farms	% Of Total Farms	% Of Total Horses Sold
1 to 3	35	36.1%	6.3%
4 to 10	26	26.8	13.7
11 to 20	20	20.6	26.5
21 to 30	9	9.3	20.2
More than 30	7	7.2	33.3
Total	97	100.0%	100.0%

4. What was the gross income received from the sale of weanlings, yearlings, and two year-old equines that were sold in calendar year 2010 by this operation?

[Open-response question: LRC staff compiled the responses into categories.]

Sales Income	Farms	% Of Total Farms	% Of Total Income
\$25,000 or less	23	24.8%	0.3%
\$25,001 to \$100,000	20	21.6	1.0
\$100,001 to \$250,000	19	20.5	3.4
\$250,001 to \$1,000,000	17	18.3	7.5
\$1,000,001 to \$3,000,000	8	8.6	12.8
\$3,000,001 to \$10,000,000	3	3.2	15.9
More than \$10,000,000	3	3.2	59.1
Total	93	100.0%	100.0%

Appendix C

Thoroughbred Breeding Incentive Fund Awards

Current Awards Structure

The table below shows the current awards structure for the Thoroughbred Breeding Incentive Fund. The program consists of five programs, which target different types of races and races in different locations.

Thoroughbred Breeding Incentive Fund Award Structure

Component	Race	Award Amount	Limit/Description
Kentucky First	Maiden special weight, Allowance, and Stakes	25% of winner's earnings	\$10,000 maximum
National	Maiden special weight and Allowance	10% of winner's earnings	\$10,000 maximum
Kentucky Grade I	<ul style="list-style-type: none"> • Grade I • Kentucky Derby and Oaks 	\$25,000 \$100,000	
National Grade I	Grade I	\$2,500	
Kentucky Claiming	Claiming	<ul style="list-style-type: none"> • \$100,000 total \$25,000/track • \$100,000 total 1st - \$50,000 2nd - \$30,000 3rd - \$20,000 	Highest earning claiming horse at each of 4 tracks Top 3 horses based on Kentucky claiming earnings

Source: Kentucky Horse Racing Commission; 810 KAR 1:070.

Kentucky First

The Kentucky First Component provides awards for maiden special weight, allowance, or stakes races run in Kentucky. Maiden special weight races are among the top races for maiden horses—those that have yet to win their first race. Allowance races require horses to meet specific weights carried by the horse or conditions to enter the race, such as age or gender. The weight a horse carries may differ depending on the horse's record. Stakes races are the top horse races. Stakes races are classified into three grades with Grade I being the most competitive.

The Kentucky First Component provides an award of 25 percent of the winner's earnings, with an upper limit of \$10,000 per race. Under this component, awards are not made for Breeders' Cup World Thoroughbred Championship races or any Grade I Stakes races run in Kentucky.

National

The National Component pays an award to the breeder of the qualified winner of each maiden special weight or allowance race won by 2-, 3-, and 4-year-old Thoroughbreds in any state other than Kentucky. The amount of the award is 10 percent of the winner's earnings, with an upper limit of \$10,000.

Kentucky Grade I Stakes Race

The Kentucky Grade I Stakes Race Component provides a \$25,000 award that is available to the breeder of the qualified winner of each Grade I stakes race run in Kentucky, excluding any Breeders' Cup World Thoroughbred Championship race run in Kentucky, the Kentucky Derby, and the Kentucky Oaks. The breeder of a qualified winner of the Kentucky Derby or the Kentucky Oaks is eligible for an award of \$100,000 for each race.

National Grade I Stakes Race

The National Grade I Stakes Race Component pays \$2,500 to the breeder of a qualified winner of each Grade I stakes race run outside of Kentucky, excluding any Breeders' Cup World Thoroughbred Championship race.

Kentucky Claiming

Each horse running in a claiming race has a set price. Any person may place a claim on the horse for the stated price prior to the race. Once the race is complete, this person would own the horse. The Kentucky Claiming Component has two parts.

The first part is a \$25,000 award to the breeder of the qualified claiming horse that has the highest earnings from claiming races during a calendar year at each of the following tracks: Churchill Downs, Ellis Park, Keeneland, and Turfway Park.

The second part of the Kentucky Claiming Component is the Kentucky claiming title award. This part of the claiming component distributes \$100,000 to the breeders of the top three Kentucky claiming horses with the highest earnings from Kentucky claiming races. The winner of the Kentucky Claiming title receives a \$50,000 award, the second-place finisher receives a \$30,000 award, and the third-place finisher receives a \$20,000 award.

Bonus Awards

If the Kentucky Breeders Incentive Fund has money remaining after the initial awards and contributions to the reserve fund, the Horse Racing Commission will make bonus awards. The following table shows the maximum awards for specific types of races. Bonus awards can be based on races in Kentucky, other states, or other countries. International Stake races are classified into three groups based on competitiveness. The groups are similar to Graded Stakes races in the US.

Kentucky Thoroughbred Breeders Incentive Fund Bonus Awards

Race		Maximum Award
International	Group 1	\$2,500
	Group 2 & 3	5,000
National	Grade I	5,000
	Grade II & III	5,000
Kentucky	Grade II & III	25,000 per race

Source: Kentucky Horse Racing Commission; 810 KAR 1:070.

Proposed Changes To Award Structure

In 2010, the Horse Racing Commission created an advisory committee to review how awards are provided under the Kentucky Thoroughbred Breeders Incentive Fund. Based on the committee's recommendations, the commission has amended the administrative regulations related to the Thoroughbred Breeders Incentive Fund. These changes will go into effect in November 2011. The table below summarizes the proposed changes.

Proposed Changes To The Thoroughbred Breeders Incentive Fund Award Structure

Race		Maximum Award
Kentucky	Derby and Oaks	\$50,000
	Grade I Stakes	\$7,500
	Grade II and III Stakes	\$5,000
	Nongraded Stakes	10% (\$4,000)
	Maiden Special Weight and Allowance	10% (\$3,000)
	Claiming Title	Top 20 claiming horses based on wins, awards range from \$20,000 to \$6,000.
National	Grade I	\$7,500
	Grade II and III Stakes	\$5,000
	Nongraded Stakes	10% (\$4,000)
	Maiden Special Weight and Allowance	10% (\$3,000)
International	Group 1	\$7,500
	Group 2 and 3	\$5,000

Source: Kentucky Horse Racing Commission.

Under the proposed changes, awards for the Kentucky Derby and the Kentucky Oaks would be decreased from \$100,000 to \$50,000.

Awards for claiming races would be distributed to breeders based on the performance of a larger number of horses. Currently, awards are provided to the top claiming horse at each track and for the top three claiming horses for the state. The proposed change would provide awards based on the 20 claiming horses with the most wins. The breeder of the top claiming horse would receive \$20,000. Awards for the other top 19 claiming horses would decrease based on their rank within the top 20. The total amount of awards for claiming horses would remain at \$200,000.

Currently, higher awards are paid for Kentucky races than for equivalent races outside Kentucky. The proposal would eliminate differences between the awards paid for maiden special weight and allowance races run in Kentucky and equivalent races run outside Kentucky. Also, the proposed change would add an award for nongraded stakes races held outside Kentucky and institute similar awards for this type of race anywhere in the US.