
**MARYLAND LOTTERY and
GAMING CONTROL COMMISSION**

1800 Washington Blvd., Suite 330, Baltimore, Maryland 21230

COMMISSION REPORT



Old Bay Gaming and Racing, LLC

OPERATION LICENSE APPLICANT

Report Date: November 7, 2016

Public Report

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Introduction

As a prerequisite to being eligible for a video lottery facility operation license (“operation license”), an applicant for an operation license must submit a Video Lottery Operation License Application to the Maryland Lottery and Gaming Control Commission (“the Commission”). The applicant must prove to the Commission, by clear and convincing evidence, that it meets the qualification criteria set forth in the Annotated Code of Maryland, State Gov’t Article (“SG”), § 9-1A-01, *et seq.* (“the Gaming Law”). Specifically, the applicant must prove that it is qualified under SG § 9-1A-07(c)(7)(i) through (v), and not disqualified under SG § 9-1A-08(d). SG § 9-1A-15. An applicant must provide all information to the Commission that is necessary for a qualification determination as to the applicant, its principals, and its principal entities.

The Maryland Lottery and Gaming Control Agency (“MLGCA,” “we” or “our”), conducted a suitability background license investigation of Old Bay Gaming and Racing, LLC (“the Applicant” or “the Company”) in connection with its application for an operation license.

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Purchase of Ocean Downs Casino and Racetrack

In July 2016, Churchill Downs entered into a joint venture with Saratoga Harness Racing, Inc. to purchase all of the equity interests of Ocean Enterprise 589, LLC, Ocean Downs, LLC, and Racing Services, LLC, which collectively own and operate the Casino at Ocean Downs and Ocean Downs Racetrack. To facilitate the purchase, Churchill Downs and Saratoga formed Old Bay Gaming and Racing, LLC on July 25, 2016. Old Bay is owned 50% by HCRH, LLC and 50% by Saratoga Casino Holdings, LLC. HCRH, LLC is a wholly-owned subsidiary of Churchill Downs, Inc. Saratoga Casino Holdings, LLC is owned 74% by Saratoga Harness Racing, Inc., 1% by Saratoga Casino Group, Inc., and 25% by Churchill Downs. By virtue of its 25% ownership interest in Saratoga Casino Holdings, Churchill Downs will effectively own 62.5% of Old Bay Gaming and Racing. Old Bay Gaming and Racing, LLC has filed a Video Lottery Operation License Application with the MLGCA.

The various parties to the purchase transaction entered into a Limited Liability Company Interest Purchase Agreement dated August 2, 2016. Under the Agreement, Old Bay Gaming and Racing will acquire a 100% ownership interest in Ocean Enterprise 589, LLC, Ocean Downs, LLC, and Racing Services, LLC.

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To finance the transaction, Old Bay has obtained a Senior Secured Credit Facility and Revolving Credit Facility.

Churchill Downs, Inc.

Background

Churchill Downs, Inc. (“CDI” or “the Company”) was incorporated in Delaware on October 10, 1990. The Company and its wholly-owned subsidiaries HCRH, LLC and MVGR, LLC primarily provide pari-mutuel horseracing, casino gaming, and online account wagering on horseracing.

Churchill Downs, Inc.’s main offices are located at 600 North Hurstbourne Parkway in Louisville, Kentucky.

Ownership of Applicant

Churchill Downs, Inc. is publically-traded on the NASDAQ under the symbol “CHDN.” In its Proxy Statement (Schedule 14A) filed with the U.S. Securities and Exchange Commission on March 29, 2016, the Company disclosed that as of February 26, 2016, it had approximately 16.6 million shares of common stock outstanding. The following individuals and entities held beneficial ownership of more than 5% of the Company’s common stock as of February 26, 2016:

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- Richard L. Duchossois – 2,306,561 shares (13.90%)
- Craig J. Duchossois – 2,158,160 shares (13.01%)
- The Duchossois Group, Inc. – 2,003,373 shares (12.07%)
- Three Bays Capital LP – 1,372,186 shares (8.27%)
- PAR Capital Management, Inc. – 1,287,144 shares (7.76%)
- Balyasny Asset Management – 1,095,003 shares (6.60%)
- GAMCO Investors, Inc. – 950,078 shares (5.73%)
- The Vanguard Group, Inc. – 947,094 shares (5.72%)

Churchill Downs, Inc. and HCRH, LLC have filed a Principal Entity Disclosure Form with the Commission. Additionally, Mr. Richard Duchossois and Mr. Craig Duchossois have filed a Principal Employee Application with the Commission.

Saratoga Harness Racing, Inc.

Background

Saratoga Harness Racing, Inc. (“SHRI” or the “Company”) traces its racing history to June 26, 1941 when it ran its first racing program at Saratoga Harness racetrack. The Company was incorporated in New York on November 30, 1986 under the name Upstate Harness Racing, Inc., and subsequently changed its name to Saratoga Harness Racing, Inc.

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Saratoga Harness Racing, Inc. is the parent company of its wholly-owned subsidiary Saratoga Casino Group, Inc. and the majority owner of Saratoga Casino Holdings, LLC. Both Saratoga Harness Racing, Inc. and Saratoga Casino Holdings, LLC have filed a Principal Entity Disclosure Form with the Maryland Lottery and Gaming Control Agency.

Ownership of Applicant

Saratoga Harness Racing, Inc. is a privately held company. Its stock consists of 2,016 Class “A” voting shares, and 25,046 shares of Class “B” non-voting shares. The following individuals held beneficial ownership of more than 5% of the Company’s Class “A” voting shares as of August 23, 2016:

- Daniel Gerrity – 1,007 shares of Class “A” (49.95%)
- Vera Belger – 505 shares of Class “A” (25.05%)
- George Featherstonhaugh – 400 shares of Class “A” (19.84%)

Each of these individuals have filed a Principal Employee Application with the Commission.

Equity Purchase by Churchill Downs, Inc.

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In June 2014, Churchill Downs, Inc. (CDI) and Saratoga Harness Racing, Inc. entered into an agreement whereby CDI agreed to purchase 25% of the shares of SHRI for approximately \$30.6 million. To facilitate the sale, SHRI created a new limited liability company Saratoga Casino Holdings, LLC (SCH), and transferred the vast majority of its assets and liabilities to SCH in exchange for 100% of the membership interests in SCH. After receiving required regulatory approvals, SHRI sold 25% of its membership interest in SCH to Churchill Downs. SHRI then distributed the net proceeds of the sale to its shareholders. SHRI and CDI also entered into a management agreement for CDI to manage the Saratoga and Colorado operations of SHRI.

Discussion of Financial Performance

We performed a detailed analysis of Churchill Downs, Inc.'s and Saratoga Harness Racing, Inc.'s operating performance and financial condition for the calendar years ending December 31, 2011 through December 31, 2015. We reviewed the following:

Revenue and Cost of Goods Sold –

Operating Expenses and Net Income

Assets, Liabilities and Shareholder Equity

Liquidity and Cash Flow

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Long-Term Debt

Trend Analysis and Comparative Performance

- **Current Ratio and Quick Ratio**
- **Operating Profit Margin and Net Profit Margin**
- **Return on Equity and Return on Assets**
- **Debt to Equity Ratio and Debt Ratio**
- **Interest Coverage Ratio**

Independent Audit of Annual Consolidated Financial Statements

Dun & Bradstreet

Tax Returns

Litigation

Financial Analysis

Overall, Churchill Downs, Inc.'s and Saratoga Harness Racing, Inc.'s operating performance and financial position can be characterized as consistently positive.

FINDINGS

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The MLGCA conducted a complete and thorough background investigation as authorized under the Gaming Law by analyzing corporate records and documents, scrutinizing the business operations, practices, and transactions of Churchill Downs, Inc.'s and Saratoga Harness Racing, Inc.'s, the parent companies of Old Bay Gaming and Racing, LLC, and conducting interviews of key personnel, focusing on required qualification criteria involving integrity and financial stability. MLGCA adhered to well-defined and approved investigative protocols in assembling the factual information incorporated in this report. The results of the investigation for the specific qualification criteria enunciated in SG §§ 9-1A-07(c)(7), 9-1A-08(d), and 9-1A-15 are summarized as follows:

1) Financial stability, integrity and responsibility

A comprehensive review was conducted of all of the consolidated financial statements for the last five years. The Applicant satisfies the standards for financial stability, integrity and responsibility. MLGCA also concludes that the individual qualifiers (principals) satisfy the Gaming Law's qualification criteria in connection with the Operation License Application.

2) Integrity of financial backers, investors, mortgages, bondholders, and other holders of indebtedness

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Based on our review, there are no material issues involving the known financial backers of the Applicant.

3) Good character, honesty, and integrity

MLGCA found that the Applicant possesses the requisite good character, honesty and integrity. No significant issues surfaced concerning the qualifications of the Applicant or its individual qualifiers. There were no material issues discovered pertaining to the Applicant's record of regulatory compliance or litigation matters.

4) Sufficient business ability and experience

Churchill Downs, Inc. and its subsidiaries have provided pari-mutuel horseracing, casino gaming, and online account wagering on horseracing since October 1990. Saratoga Harness Racing, Inc.'s has provided pari-mutuel horseracing since June 1941. Since then, video lottery gaming has been approved at its New York racetracks. Therefore, the Applicant clearly possesses the requisite business ability and experience.

5) Potential Disqualifying factors

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The Applicant is not disqualified from being issued an operation license based on any of the criteria listed in SG § 9-1A-08(d). The Applicant is qualified to be awarded a license by the Commission.

APPLICANT and PRINCIPAL ENTITIES

The Applicant and its principal entities satisfy the applicable qualification criteria under SG § 9-1A-07(c)(7), and are not disqualified under SG § 9-1A-08(d).

1. Old Bay Gaming and Racing, LLC.
2. Churchill Downs, Inc.
3. HCRH, LLC
4. Saratoga Harness Racing, Inc.
5. Saratoga Casino Holdings, LLC

PRINCIPAL QUALIFIERS

We identified the following natural person qualifiers (“principals”) who are associated with the Applicant and its principal entities. We conducted an extensive due diligence investigation on each qualifier, as described in our full report. We found that these principals have satisfied the applicable

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qualification criteria under SG § 9-1A-07(c)(7), and that none are disqualified under SG § 9-1A-08(d).

1. Vera Belger (Saratoga Harness Racing, Inc.)
2. Daniel Gerrity (Saratoga Harness Racing, Inc.)
3. George Featherstonhaugh (Saratoga Harness Racing, Inc.)
4. James Featherstonhaugh (Saratoga Harness Racing, Inc.)
5. Gary Keehfus (Saratoga Harness Racing, Inc.)
6. Marcia Dall (Churchill Downs, Inc.)
7. Duncan McConnell (Churchill Downs, Inc.)
8. Austin Miller (Churchill Downs, Inc.)
9. William Mudd (Churchill Downs, Inc.)
10. Richard Duchossois (Churchill Downs, Inc.)
11. Craig Duchossois (Churchill Downs, Inc.)

CONCLUSIONS and OPINION

MLGCA's investigation has confirmed that the Applicant has sufficient financial resources and found no derogatory information regarding the Applicant's qualifications. Based on the criteria in SG §§ 9-1A-07(c)(7) and 9-1A-08(d), we conclude that the Applicant, its principal entities, and

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principals, have established by clear and convincing evidence their qualifications for an operation license.