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Case No: CO/523/03

IN THE HIGH COURT OF JUSTICE
ADMINISTRATIVE COURT

Royal Courts of Justice
Strand, London, WC2A 2LL

31st July 2003

B e f o r e :

THE HONOURABLE MR JUSTICE HOOPER

Between:

The Queen on the Application of Sporting Options plc **Claimant**

- and -

The Horserace Betting Levy Board. **Defendant**

HTML VERSION OF JUDGMENT : APPROVED BY THE COURT FOR HANDING DOWN (SUBJECT TO EDITORIAL CORRECTIONS)

Mr Justice Hooper

1. This is an application for judicial review of the defendant's decision on 31 October 2002 setting the horse race betting levy to be paid by betting exchanges during the period covered by the 42nd levy scheme, which runs from April 1 2003 to 31 March 2004. Under this scheme, the claimant, a betting exchange, is required to pay for the period covered by the scheme, a levy of 10% of the gross profits achieved through the claimant by individual successful layers on British horseracing during that period, with no offset for any losses made by such persons backing horses or for any losses made by such persons laying horses through other exchanges. Under the 41st scheme which covered the previous year and which had been determined not by the defendant but by the Secretary of State in February 2002, betting exchanges had been required to pay a levy of 10% of the gross commission earned by it from its customers. That commission was earned by deducting an average of 2.2% from the winnings of a subscriber on an individual event (race, match etc) for which the exchange provided the facility to bet.

2. Betting exchanges such as the claimant are very new. Without the internet and without sophisticated software, they could not exist. At the time of the decision the leading betting exchange was the Sporting Exchange Limited which trades as "Betfair". It held 90% of the betting exchange market and had come into existence in June 2000.

3. The claimant was founded by Mr Griffiths, an ex-trader in equity derivatives from Barclays de Zoete Wedd, with a colleague from that institution. Following a substantial investment of money and time, including the development of the software which was not available for purchase, it started trading in May 2002.

4. Judicial review proceedings to challenge the 42nd Levy in so far as betting exchanges were concerned were threatened by Betfair. When it became clear that Betfair did not intend to proceed, the claimant started judicial review proceedings on the last day of the three-month period. The parties subsequently sensibly agreed, during the application for permission hearing, that permission should be granted limited only to declaratory relief and upon an undertaking by the claimant that in any event it would pay during the period covered by the 42nd scheme any sums which would have been due on the basis used under the 41st scheme. It was agreed during the course of argument that I should reach my conclusions on the challenges and that, if the claimant were to be successful, there would be a hearing to consider what relief, if any, should be granted.

Betting Exchanges

5. In paragraphs 4 and 6 of his first witness statement (1/67) Mr Griffiths gave this description of the sports betting business, excluding betting exchanges and firms engaged in internet spread betting.

> "4. The customary way in which a person can gamble on the outcome of a sporting event in this country is to place a bet with a traditional bookmaker. The better places a bet with the bookmaker by paying him a stake and receiving odds on the outcome of the event desired. If that outcome occurred, the bookmaker pays to the better out of his own funds the winnings, being the stake multiplied by the odds. There are currently four common forms of bookmakers:
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> large chains of bookmakers such as Ladbroke Racing Ltd, Coral Racing Ltd and William Hill Organisation Ltd who each have a large network of high street shops, a substantial infrastructure, internet sites which allow such bets to be placed on-line and services which allow bets to be placed over the telephone;
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> small high street bookmakers with an individual shop or small chains of shops; and
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> internet-only bookmakers such as Blue Square;
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> on-course bookmakers who tend to be sole proprietors.
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> 6. All these bookmakers, although diverse in their businesses, operate effectively in the same way. They calculate the odds for the outcome of a sporting event, allow bets to be placed on such outcomes according to the odds they calculate and take the risk of paying out the winnings if the outcome bet upon arises. Calculating the odds is a matter of highly skilled expertise. The large bookmaking firms in particular employ (at great expense) many people who are responsible for calculating these odds.

6. Mr Griffiths describes, in paragraph 7, how betting exchanges operate.

"In the past three years, a completely new form of betting business has been developed known as "bet brokers" or "betting exchanges". With a betting exchange, the business does not enter into the bet with the better at all, but merely facilitates the better to enter into a bet with another person, unrelated to the business. When a better seeks to enter into a bet, he can do so either as a "backer", that is betting that a particular outcome will occur, or as a "layer", that is betting that a particular outcome will not occur. In this way, the backer enters into the traditional role of the gambler and the layer enters into the traditional role of the bookmaker. Accordingly, the betting exchange business takes no risk in the bet. The risk lies between the backer and the layer. The betting exchange makes its money solely by charging commission on the winner of the bet [whether backer or layer] for having brokered the transaction by introducing the backer and the layer to each other. "

7. In paragraph 8 Mr Griffiths describes the advantages as he sees them of betting exchanges:

"A betting exchange business offers three advantages to betters as follows:

Because the betting exchange does not enter into any bet itself, it does not have to enter into the complex process of calculating odds on the outcome of a sporting event. The odds are purely a matter for the respective betters, the backer and the layer. This saves the betting exchange very substantial costs and means that it can provide the service at a very significantly lower net cost than traditional bookmakers.

A better has the option of being a layer as well as a backer. With a traditional bookmaker, the better can be only a backer.

Once a bet has been entered into between a backer and a layer on a betting exchange service, either party may then seek to trade his position as the odds change.

For example, if a backer bets £10 that Horse A will win a race at odds of 2 to 1, he may subsequently be able to lay (that is bet against) the same amount on the same horse at shorter odds, of say 6 to 4. If the horse wins, he receives £20 for the bet where he was a backer and pays £15 for the bet where he was a layer, meaning that he wins £5 overall. Conversely, if the horse loses, he makes and loses £10 so he breaks even overall.

Typically, an individual may enter into a number of individual bets on one aspect of the outcome of a sporting event. This process in itself adds to the challenge and excitement of betting for some betters."

8. On the then website, Sporting Options told those who visited the site, amongst other things:

"6. Be the Bookie: Sporting Options has a 'Be the Bookie' feature that allows you to 'lay' multiple bets in a single process. To use this facility you would select your maximum payout and your odds for each selection in a betting market. 'Be the Bookie' will automatically calculate the various backers stakes you would need to 'lay' in order to achieve a proportionate set of prices. The system also calculates the guaranteed percentage return associated with your chosen prices. Please see the 'Betting Help' for a more detailed description of Be the Bookie."

> 8. Liquidity: Betting 'liquidity' or betting volume is vital to the success of a betting exchange. Sporting Options has carried out months of negotiations with several key groups of liquidity providers. These groups include numerous independent bookmakers both on and off-course, several on-line bookmakers, and many former City of London colleagues who enjoy trading sporting and financial markets on a regular basis."

9. In paragraph 9 he describes what he sees as a difficulty for betting exchanges:

> "The disadvantage for a betting exchange to betters is that sometimes there may not - at any one time - be a counterpart better prepared to take a particular bet (a backer may not be able to find a layer or vice versa). By contrast, a bookmaker will always be prepared to accept a bet, albeit only at the odds he sets. This disadvantage is particularly acute with a small betting exchange business which has fewer members. This is one reason why any betting exchange starting up seeks to build up a substantial subscriber base as soon as possible."

Spread betting

10. Spread betting is described by Mr Brack in paragraph 11 of his second witness statement (1/117):

> "A further category of bookmaker is the companies that engage in spread betting. Spread betting involves betting on the outcome of a financial or sporting event based on a "spread" quoted by the bookmaker. The "spread" is a range of values (say, a range of between 150 and 200 runs for a cricket team score). The customer chooses whether they predict that the actual outcome will be above or below that spread. If they predict it will be above the spread then they "buy" at the top of the spread by staking an amount on the score being above the spread. If the customer is right and the end total is above the spread upper limit (in my example, if more than 200 runs are scored), the customer wins an amount which is equal to the value of their stake multiplied by the difference between the final total and the upper limit of the spread (in my example, if the score was 250 runs, the winnings would be 50 multiplied by the value of the stake). If on the other hand the customer is wrong, then, conversely, they pay an amount equal to their stake multiplied by the difference between the top of the spread and the actual total. The same principles apply (but in reverse), if the customer predicts that the outcome will be below the spread in which case they "sell" at the bottom of the spread. The customer can also sell his "bet" during the course of a game, before the final total is ascertained (e.g. before the end of the cricket team's innings) for a market price which will reflect how far above or below the spread the final total appears to be reaching."

11. Unlike betting exchanges, spread betting firms have their own trade association.

Are betting exchanges "bookmakers"?

12. There has been some debate whether betting exchanges (and also spread betting firms) are bookmakers as defined in section 55 of the Betting, Gaming and Lotteries Act 1963 ("the 1963 Act") and thus require a permit under section 2 of the Act to operate lawfully. The definition of "bookmaker" in section 55 reads:

> "bookmaker" means any person other then the Totalisator Board who --

(a) whether on his own account or as servant or agent to any other person, carries on, whether occasionally or regularly, the business of receiving or negotiating bets or conducting pool betting operations; .."

Betfair had apparently insisted that it was not a bookmaker (3/185). The betting exchanges, including Betfair, have, in fact, applied for and been granted permits as bookmakers. As such they are liable to pay the horserace betting levy.

13. There has also been a more heated debate about whether those who lay bets on betting exchanges fall within the definition of bookmakers and thus require a permit. To the extent to which permit-holding bookmakers use the exchanges to lay bets there is no problem. Whether the others or some of the others fall within the definition of bookmaker remains an issue, although no proceedings have been taken against such layers for aiding and abetting unlawful bookmaking. The traditional bookmakers have argued vociferously that layers on betting exchanges are bookmakers and are required to obtain a permit (see paragraph 16 of witness statement of Mr Williams). At a meeting of the Board on 12 September, Mr Ross (an observer from the Committee) said that the Committee had received legal advice to the effect that, in the context of betting exchanges, the activity of the layer was illegal and, therefore, the activities of the bettor and Betting Exchange operator were illegal too. I should add that the current view of the Department as expressed in an April 2003 position paper (3/71, at 80-81) is that exchange users who are layers should not need to be licensed to achieve the Government's regulatory objectives.

The structure and responsibilities of the Horserace Betting Levy Board and the Bookmakers' Committee

14. I turn to the structure which governs the defendant Board and the Bookmakers' Committee, the interested party which, through Mr Vajda QC, seeks to uphold the challenged decision of the defendant and who adopted the defendant's arguments. The effect of the structure is that the Committee's recommendations require approval by the Board and the Board can approve only recommendations made by the Committee. If no "agreement" can be reached by midnight on October 31, the Secretary of State determines the scheme (as happened for the period 2002-2003).

15. Section 24 of the 1963 Act provides:

"(1) There shall be a Horserace Betting Levy Board (in this Act referred to as 'the Levy Board') which shall be charged with the duty of assessing and collecting in accordance with the subsequent provisions of this Part of this Act, and of applying, subject to those provisions, for purposes conducive to any one or more of the following, that is to say—

(a) the improvement of breeds of horses;

(b) the advancement or encouragement of veterinary science or veterinary education;

(c) the improvement of horse racing,

monetary contributions from bookmakers and the Totalisator Board.

(2) The Levy Board shall consist of a chairman and seven other members of whom:

(a) the chairman and two other members shall be appointed by the Secretary of State and be persons who the Secretary of State is satisfied have no interests connected with horse racing which might hinder them from discharging their functions as members of the Board in an impartial manner;

(b) three members shall be appointed by the Jockey Club (incorporating the National Hunt Committee);

(d) one member shall be the chairman for the time being of the Bookmakers' Committee; and

(e) one member shall be the chairman for the time being of the Totalisator Board."

The membership at the time of the challenged decision was made up as follows:

(1) Mr Robert Hughes, Chairman – Formerly in local government, including 10 years as Chief Executive of Kirklees Metropolitan Council;

(2) Sir John Robb, Deputy Chairman – Formerly Chairman of British Energy, Chairman of Wellcome Plc and Chief Executive of Beechams;

(3) Mr Keith Elliot – Expert sports writer contributing form guides, formerly a lecturer in economics;

(4) Mr Warwick Bartlett – Chairman of the Bookmakers' Committee, Chairman of the Association of British Bookmakers, consultant on the British gaming industry, formerly Chairman of the British Betting Offices Association;

(5) Mr Keith Brown – Chairman of the Racecourse Association, racehorse owner, formerly a managing director of a merchant bank;

(6) Mr Peter Jones – Chairman of the Horserace Totalisator Board [the "Tote"], formerly director of an international advertising agency;

(7) Sir Eric Parker – Member of the British Horseracing Board Ltd [the "BHB"], formerly Chairman of the Racehorse Owners Association an Chairman of Trafalgar House Plc; and

(8) Mr Tristram Ricketts – Secretary General of the BHB, formerly Chief Executive of the HBLB.

At the meeting of 31 October Mr N Smith attended in the place of Mr K Brown. Mr Rodney Brack is the chief executive. Another member of the Committee, Mr Ross, would attend as an observer, in accordance with a well established practice (see 1/169G).

16. Section 27 provides:

(1) The contributions such as are mentioned in section 24(1) of this Act to be made by bookmakers shall be paid by way of a levy in respect of each levy period in accordance with a scheme having effect for that period under this

section; and in this Act the expression "levy period" means a period of twelve months beginning with 1st April in any year.

(2) Any such scheme shall include provision—

(a) for securing that the levy shall be payable only by a bookmaker who carries on on his own account a business which includes the effecting of betting transactions on horse races, and only in respect of so much of the business of the bookmaker as relates to such betting transactions;

(b) for bookmakers to be divided for the purposes of the levy into different categories;

(c) for the amount, if any, payable by way of the levy by any particular bookmaker to be determined by reference to the category into which he falls;

(d) as to the method of the promulgation of the scheme by the Levy Board;

...

(3) Not later than such date before the beginning of any levy period as the Levy Board may determine, the Bookmakers' Committee shall make recommendations to the Levy Board with respect to the scheme to have effect under this section for that period, and those recommendations shall take the form either of a draft scheme or of a recommendation that the current scheme shall continue to have effect without amendment or with specified amendments.

(4) If the Levy Board approve the recommendations aforesaid, or those recommendations as revised by the Bookmakers' Committee in the light of any observations thereon made to the committee by the Board, the scheme so recommended and approved shall have effect accordingly for the levy period in question."

17. By section 1 of the Horserace Betting Levy Act 1969, if five months before the beginning of a levy period the Defendant has not approved recommendations or revised recommendations of the BC, the Defendant must forthwith report the circumstances to the Secretary of State and the Secretary of State must determine the scheme to have effect.

18. Section 26 (1) makes provision for the Bookmakers' Committee.

"For the purposes of the contributions such as are mentioned in section 24(1) of this Act to be made by bookmakers, there shall be a committee, which shall be known as the Bookmakers' Committee, constituted in such manner as the Secretary of State may, after consultation with any body appearing to him to be representative of the interests of bookmakers generally, by regulations made by statutory instrument provide."

19. By virtue of regulation 2 of the Horserace Betting Levy (Bookmakers' Committee) Regulations 1999, 1999 No. 1468 which came into force on 15th June 1999, the Committee consists of 12 members of whom:

"(a) two shall be appointed by Coral Racing Ltd;

(b) two shall be appointed by Ladbroke Racing Ltd;

(c) two shall be appointed by William Hill Organisation Ltd;

(d) two shall be appointed by the Betting Office Licensees Association Ltd to represent the interests of the members of that body other than those listed in paragraphs (a) to (c) above;

(e) two shall be appointed by the National Association of Bookmakers Ltd from amongst persons nominated for the purpose by associations for the time being affiliated to the National Association of Bookmakers Ltd; and

(f) two shall be appointed by the British Betting Office Association Ltd."

The organisations referred to in (d) and (f) have now merged. Mr Bartlett is and was at the time of the challenged decision, Chairman of the Committee. He was and is still a member of the Board.

20. The Bookmakers' Committee represents, as it is now constituted, what can aptly be described as the traditional on course and off course bookmakers. The betting exchanges and the spread betting firms were not represented either individually or through their own or one of the named trade associations. Betfair has now made submissions to the Secretary of State that it should be made a member.

21. In his first witness statement Mr Bartlett described the function of the Committee in the following way (paragraph 13 at 1/163):

> "... the Committee has a statutory responsibility to make recommendations on behalf of the industry as a whole and as Chairman, I am conscious of the requirement for the Committee's recommendations to be based on a detailed and balanced assessment of what is a fair and reasonable contribution from each sector of the industry."

22. Mr Pannick QC, on behalf of the Board, accepted this as a correct description. During the course of argument he had stated that, in the view of the Board, the Committee should inform the Board of all relevant matters concerning the interests of all bookmakers. He withdrew that statement having given further consideration to this passage from Mr Bartlett's statement. Both Mr Vajda and Mr Pannick, referring to this passage, submitted that it is the Committee's task, in so far as the Board is concerned, to forward their recommendations with any supporting reasons which they might wish to have considered. The Committee has no obligation, they submitted, to forward the views of those in the industry who did not or would not support the recommendations.

23. That this is the approach adopted by the Committee is shown by what happened to a draft letter to the Board dated 30 October (352) prepared by Group Captain Nixon, Secretary to the Bookmakers' Committee, to accompany the "final" recommendations to the Board. The letter included for the Board a summary of the position of the sporting exchanges on the Committee's recommendations which concerned them. It was "collectively decided" at the meeting in the afternoon of 30 October to delete, amongst other things, that summary (see 3/207) because it was the Committee's role to make recommendations rather than set out the views of those to whom they had talked. (See third witness statement of Mr Bartlett). The draft letter was produced by the Committee for the first time during the hearing before me.

<u>Events leading up to the adoption of the 42nd Scheme</u>

24. I turn to the events leading up to the adoption of the 42nd scheme.

25. On 5 September, the Committee sent a letter (see 3/136) setting out its forecasts of the anticipated levy for 2002-2003 and touching upon its proposed recommendations for 2003-2004. The letter reads in part:

> "Two major factors have emerged. There is no doubt that the increasing popularity of alternative products, including the Football World Cup, have played their part. However, we believe the main reason to be that horseracing gross win across all platforms is running at about 1% less than we might have expected, almost certainly because money which might otherwise have been channelled through these platforms is being diverted through the betting exchanges. This effect has become much more pronounced since Betfair and Flutter.com merged earlier this year.
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> …
>
> It is a fact that the on-course market is being influenced by some bookmakers laying off their liabilities through the exchanges, thus enabling them to sustain a bigger price about a horse than the local market can justify. The effect is to reduce the off-course margin by artificially inflating the SP.
>
> …
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> A further effect of diverting money through the betting exchanges is to reduce the amount of revenue which that money would otherwise have generated for the levy and for racing. This is because the gross profit margin on which the exchanges pay levy is very much lower than that of a commercial bookmaker. If we assume that the exchanges charge, on average, 4% commission and that this is their sole source of income, then their gross profit margin is 4%; this compares with a combined average margin of around 12.5% across the LBO, telephone and internet channels of other bookmakers. If £1.3M in levy is derived from 10% of a 4% margin, it follows that up to an additional £2.76M would have been payable had that money been channelled through the conventional platforms. If the betting exchange gross margin were 3%, up to £4.1M extra would have been payable.
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> It is therefore likely that between £3M and £4M of the theoretical £6M deficit is directly attributable to the diversion of money through the exchanges. Alternatively, it is arguable that the whole shortfall is due to the reduction in overall margin resulting from the activities of the betting exchanges.
>
> The Committee will be seeking to alleviate the negative effect on the levy and the income to racing in general which the betting exchanges are having by making recommendations which address the liability of those who profit by laying bets through the exchanges, as well as that of the exchanges themselves."

26. Mr Brack, chief executive of the Board, sets out the usual procedure for determining the levy in paragraph 29 of his second statement (1/126):

> "Generally, the first recommendations are submitted by the Bookmakers' Committee in September and these are considered by the HBLB at its board meeting in September. It is fair to say that it is not usual for these to be accepted by the HBLB. The Bookmakers' Committee will then usually submit revised

recommendations which will be considered by the HBLB at its board meeting in October. These too are often not approved and it has not infrequently been the case that only on 31 October itself are the recommendations in a final form which the HBLB feels able to approve."

27. The Bookmakers Committee forwarded their recommendations on 12 September 2002. Recommendations are never forwarded before then according to Mr Bartlett's third witness statement. There had, by then, been no consultation with any of the betting exchanges (as to Betfair, see 3/143) nor with the spread betting firms or their Association. Making "recommendations on behalf of the industry as a whole" (to use Mr Bartlett's words) did not involve, in the view of the Committee, consultation with those likely to be affected by the recommendations but not represented on the Committee. But for the concerns of the Board, the betting exchanges would not, it appears, have been consulted by the Committee (as they were to be on 24 October).

28. In a letter dated 12 September 2002, enclosing the recommendations, Mr Bartlett wrote to the Chairman of the Board:

> "Uniquely, representatives of the Committee have been in dialogue with members of senior management at the British Horseracing Board during the drafting process and we believe that the attached document accurately reflects the agreements which have been reached between the two bodies."

During the course of the 12 September meeting of the Board, Mr Ross, a member of the Committee, said that the recommendations put forward by the Bookmakers' Committee were intended to be a mirror of the BHB commercial policy.

29. In so far as the betting exchanges were concerned, the recommendations were:

> "(iii) Betting Exchanges/Bet-Brokers. The Committee recommends that companies who derive their gross profits from operating betting exchanges or conducting bet-broking activities, should pay 10% of such gross profit in levy, where that profit arises from British horseracing. We recommend that gross profit in the case of betting exchanges should be defined as the revenue derived from their gross commission on horserace betting business deducted from the amounts paid out to bettors and bet-takers.
>
> (iv) Betting Exchange Customers. We recommend that all betting exchange customers who wish to lay bets through the facilities of a betting exchange or bet-broker should be charged levy at a flat rate of 10% on any gross profits derived from laying bets on British horseracing. In effect, this recommendation means that the charge is 10% of all layers' profits assessed on an annual basis, which equates to the extraction of all "lays" relating to British horseracing on individual accounts and assessing the profit made on those "lays" during the year; ie, there is no aggregation between individual layers. "Backs" are not taken into account and there is no provision for offsetting successful "lays" against losing "backs". Similarly, and in order to provide consistency with the tax/levy rules applied to hedging, the Committee recommends that levy liability is assessed on layers' gross profits before the deduction of commission charges. To facilitate this, we recommend that bet-brokers/betting exchange operators be responsible for carrying out the required calculations and making the appropriate payments, in addition to the levy payments as recommended at paragraph 9b(iii) above."

30. Under the proposed scheme, the exchanges were to continue to pay the 10% as they had in the year before, but profitable layers were also to pay 10% on their profits during the levy period before deduction of commission charges without being able to set off any losses made by them on backs, with the exchanges being responsible for making the necessary payments. This basis is known as the "aggregated profitable layers basis". That contrasts with the "aggregated layers basis", in which the accounts of all layers with the exchange are aggregated over the levy period, whether profitable or not. The aggregated layers basis was the basis then used by the Customs and Excise to assess the gross profits tax on betting. "Lay" and "laying", under the terms of the levy (3/254) mean "the taking of a bet by a person whereby such person offers odds and accepts the payment of a stake in respect of the outcome of a particular event."

31. Due to a "double counting error" (as the Committee saw it) which was "corrected" only at the 30 October Committee meeting, permit holding bookmakers under the September recommendations were also being required, as they had been in the previous year, to include in their gross profits, profits made on lays with the exchanges. Following the correction of the oversight, the obligation on the permit holding bookmaker to account for any aggregated profits by laying through the exchange in the 41st scheme was removed and placed on the betting exchange.

32. Let us assume, for the moment, that a betting exchange decides to meet its obligations to the Levy Board by increasing the commission on backers and layers (as both the Board and the Committee in the course of argument before me assumed it might well do). The permit holding bookmaker making a profit over the year on his exchange lays would, under the 41st scheme, have had to take that profit into account in determining how much levy he had to pay. Under the 42nd scheme he shifts some of that financial burden on to backers and layers who had made money on a particular event and thus had to pay commission (even though they may have made no profit over the levy year). I should add that the bookmaker under the 42nd scheme is not able to aggregate any laying losses when determining his gross profits. To that extent he suffers a disadvantage.

33. I should also add that bookmakers who hedge their position by backing horses were not required under either the 41st or proposed and adopted 42nd scheme to account for profits made by backing, nor could they take into account losses made on backs (see definition of "gross profit" in the Terms of the Levy, 3/253).

34. In the view of the Committee, layers on betting exchanges were, in the 42nd scheme, being equated with permit holding bookmakers, as well as the exchanges themselves. Treating layers as permit holding bookmakers was justified by the Committee in the following way in paragraph 6 of the Recommendations:

> "For the first time, the Committee will be making specific recommendations in respect of spread betting companies and betting exchanges/bet-brokers. We recognise that, under the 41st Scheme, the bet-brokers are currently required to pay levy at a rate 10% of the gross profits which they derive from the commission charged to their customers on horseracing business. However, we consider that individuals using the facilities of a betting exchange to lay bets also have an individual liability to pay levy on any gross profits they may make from horseracing and we will make recommendations to this effect; this reflects the BHB's commercial policy."

35. The reference to the BHB policy was a reference to the policy adopted by the BHB to use the 10% of gross profits as a basis for determining the licence fee which bookmakers had to pay to use the commercial data about races (runners and riders etc), for which the BHB have the rights. (See further, second witness statement of Mr Brack, paragraphs 40 and following.)

36. The demand by the BHB to the spread betting firms to make this the basis of calculating the amount to be paid was strongly opposed by the Association and was the subject of a proposed submission to the Office of Fair Trading (3/157), which was carrying out an investigation into certain aspects of the way in which the BHB runs racing. The Board knew about this investigation and the Board knew that it had not been completed before 31 October (see paragraph 15 at 3/113). The Board were told that, in the event of findings being made by the OFT that could affect the recommendations for the 42nd levy, the Committee reserved the right to withdraw the recommendations.

37. The history of the negotiations between the BHB and Betfair are set out in a letter from Betfair to the Board dated 15 October (3/145-146). Betfair wanted the licence to be based on the 41st levy basis. The BHB presented, on a take-it-or leave-it basis, a licence fee on the Customs and Excise basis for determining the gross profits tax on betting, namely the aggregated layers basis, which takes into account all layers and not just profitable layers. In May Betfair signed that agreement. Later, according to Betfair, BHB sought to "re-interpret" the agreement to base the payments on the aggregated profitable layers basis, the same basis proposed by the Committee for the 42nd levy. The following passage appears in paragraph 49 of Mr Brack's second statement (1/132):

> "At a later meeting of the HBLB on 23 October 2002, Mr Tristram Ricketts, Secretary General of the BHB, said that although a licence agreement had been signed by Betfair and returned to the BHB, the BHB had not co-signed the agreement because Betfair had not provided certain requested information. Mr Ricketts also said that "it appeared unlikely that any licence agreement with the betting exchanges would be concluded and in place before 31 October" ("RLB2" page 167)."

38. It appears that no other agreements were reached between the BHB and the spread betting firms or the betting exchanges before 31 October (as to later developments, see 2/84). It follows that, at the October 31 meeting the Board, including three BHB members, set, as the basis for the levy on the betting exchanges, the basis which the BHB was trying to obtain for the right to use the BHB data. Furthermore in the letter of 12 September, quoted earlier (paragraph 28), from the Committee to the Board with the recommendations, Mr Bartlett wrote that, uniquely, the recommendations had the approval of senior management of the BHB.

39. I should however quote a further passage from Mr Brack's second witness statement in which he submits that no adverse inferences should be drawn from this:

> "50. Press reports following the joint press release on 17 April 2002 made reference to the idea of future levy schemes mirroring the commercial arrangements between bookmakers and the BHB (see e.g. Racing Post, 18 April 2002, fourth paragraph from the end, at "RLB2" page 69). The idea that the terms of the 42nd levy scheme would mirror the terms of the data licence agreements entered into between the BHB and certain off-course bookmaking companies was well known in the industry at the time.
>
> 51. Although the anticipation of the major bookmakers had been publicly stated, this aim was not conclusive as to what terms would be adopted by the Bookmakers' Committee for recommendation to the HBLB or what would be approved by the HBLB. I refer for example to an observation made by the Chairman of the HBLB during a meeting of the HBLB on 23 October 2002. The minutes record that he:
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> "acknowledged the Committee's desire to reflect the BHB's current commercial policy, but said that it did not have any statutory force and, therefore, the HBLB

> must consider the issues from the point of view of the statutory levy process" (first paragraph on page 3 of the minutes for that meeting at "RLB2" page 166).
>
> I would respectfully invite the Court to conclude that there is no evidence that any of the board members failed to take into account their statutory and other obligations to the board when taking decisions as board members, nor put themselves (or indeed were put) in a position which could fairly be perceived as having compromised their role as board members."

40. At an earlier stage of the proceedings the claimant complained about a side agreement dated 17 April 2002, described by Mr Brack in the following way:

> "Under it, the bookmakers that were party to that agreement evidently agreed to recommend to the HBLB a levy scheme for each year which contained identical terms to, or no less favourable to the BHB than, the terms set out in the data licence. The BHB agreed in return "to support any such recommendation".

41. The claimants have abandoned the ground based on that agreement.

42. Although in the 12 September recommendations, layers on an exchange are being equated to permit holding bookmakers to justify the recommendations, the layer would, unlike the bookmaker dealing with a punter, still have to pay a commission to the betting exchange if, on any event, he made a profit taking into account both his lays and his backs (if any) and 10% of that commission would be paid by the exchange as levy.

43. One of the justifications for the recommendations (paragraph 325 above) was that "individuals using the facilities of a betting exchange to lay bets also have an individual liability to pay levy on any gross profits they may make from horseracing". As Miss Rose pointed out, section 27(2)(a) provides that "the levy shall be payable only by a bookmaker who carries on his own account a business", the word "bookmaker" being defined in section 55 of the Betting, Gaming and Lotteries Act, 1963 (see above paragraph 12). They have no such liability unless the individual is a permit holding bookmaker carrying on a business. Miss Rose argues that the scheme is therefore unlawful.

44. Correcting the double-counting error meant that the liability was shifted from the bookmaker to the exchange and, as I have pointed out, could result in the shifting of the liability to other punters, not in business and whether layers or backers (paragraph 32 above).

45. Mr Pannick, at first, submitted that the purpose of the levy was to plough back into racing "a portion of the profits of the industry" and that justified the challenged decision. He subsequently withdrew that submission.

46. The recommendations included an estimated yield:

> "Applying the recommendations described above, the Committee estimates the projected yield from the 42nd Scheme to be in the order of £94.31 million, to which may be added an allowance of up to £3.5 million for receipts from racecourse bookmakers betting exchanges and their customers, and the minimum guarantee, giving a total estimated yield of £97.81 million. However, as notified to the Board under separate cover, the Committee is aware that the effect of the betting exchanges has been to reduce the margins of bookmakers; if this trend were to continue, then it is most improbable that there will be significant growth in gross profits on horseracing next year. In that event, we would estimate the levy yield to be in the region of £93M-£94M."

47. The reference to a notification "under separate cover" is a reference to an earlier letter of 5 September 2002 from the Committee Chairman to the Board Chairman. That letter, the contents of which I have already set out (paragraph 25) expresses considerable concern about the erosion of the margins of bookmakers due to the activities of the betting exchanges.

48. Mr Brack prepared a report for the meeting of the Board on 18 September. The first item related to the anticipated yield from the 41st levy as forecast in the 5 September letter. As to these figures Mr Brack wrote:

> "2.2 These figures need to be treated with some caution since little hard information is available on the fast changing betting market this year. For example, the Committee includes in its forecast, a contribution from the Betting Exchanges of £1.3m. This implies a total Betting Exchange turnover of around £6.2m per week (a 10% levy charge on a 4% gross profit margin). Recent Press reports indicate that turnover is currently running closer to around £20m per week"

49. In so far as betting exchanges, he continues:

> "Comment
>
> 6. It is understood that commercial deals between the BHB and the on-course bookmakers and the Betting exchanges have not yet been concluded. Discussions are continuing and it is likely, therefore, that the Committee will wish to change its recommendation in respect of one or both of these activities before 31st October 2002.
>
> 6.1 …
>
> 6.2 It is unknown whether the Betting Exchanges will be able to comply with the proposed charge on layers. At the least, it will require them to change their computer and accounting systems, with a degree of complexity and attendant cost. It is suggested that this issue should be explored with the leading Betting Exchanges before the Board takes a final view."

50. The Board met to consider the 12 September recommendations on 18 September. The following note appears in the minutes immediately after the first reference to the 42nd scheme (3/121):

> "Referring to comments made earlier to members by the Minister, Mr Bartlett said that it was incumbent upon all parties to reach an agreement on the 42nd Levy Scheme, thus avoiding a referral to [the Secretary of State]. "

The minutes do not set out the Minister's comments. As I have already said, that agreement had to be reached by midnight on 31 October if there was to be no such referral.

51. In so far as the betting exchanges were concerned, the minutes record that the Chairman:

> "noted that whilst the proposals for Betting Exchanges were controversial, they resulted from due process for levy purposes. …"

52. It is not clear what the Chairman meant by this.

53. Mr Jones, Chairman of the Tote, was critical of the proposals:

> "Whilst noting THE CHAIRMAN's views, MR JONES said that he was concerned that the minority parties, within the bookmaking industry, i.e. spread betting bookmakers and Betting Exchanges, were not sufficiently represented on the Bookmakers' Committee which, in his view, was not fair. He did not think it was right that the majority views of the Committee should be imposed on those two sections of the industry to reach an agreement. The proposals were, therefore, invalid. …"

54. A little further on, the minutes read:

> "Comments then followed between THE CHAIRMAN, MR RICKETTS, MR BARTLETT AND SIR ERIC on the interpretation of, and validity of Betting Exchanges and the impact of their operation on the betting market. MR ROSS [an observer] said that the recommendations put forward by the Bookmakers' Committee were intended to be a mirror of the BHB commercial policy. He said that the legality of the activities of Betting Exchanges was a separate issue to determining the Scheme. He referred to the Minister's earlier comments that the activities of Betting Exchanges was [sic] "potentially illegal". He said that the Bookmakers' Committee had received legal advice to the effect that, in the context of Betting Exchanges, the activity of the layer was illegal and, therefore, the activities of the bettor and Betting Exchange operator were illegal too."

55. This meeting was followed up by a letter of 23 September (3/127) from the Chairman of the Board, Mr Hughes, to Mr Bartlett. In that letter the Chairman referred to vulnerability to "legal attack via an application to the Court for judicial review." A useful summary of that letter appears in paragraph 70 of Mr Brack's second witness statement (1/140):

> "Following the meeting Mr Hughes wrote to Mr Bartlett on 23 September 2002 ("RLB2" pages 127 and 128). Amongst the points which Mr Hughes made in that letter, he noted that the Bookmakers' Committee's comments in respect of enforcement of certain National Pitch Rules had been passed to the NJPC (3rd paragraph at "RLB2" page 127). He also requested the supporting statistical analysis regarding the fall in the proportion of horseracing's share of total gross profits from betting (5th paragraph at "RLB2" page 127). Mr Hughes also discussed the absence of any commercial arrangements between the BHB and three types of bookmakers; on-course bookmakers, spread betting bookmakers and betting exchanges (6th paragraph "RLB2" page 127). He also acknowledged the issue, which had been mentioned in the HBLB meeting of 18 September 2002 (see above at paragraph 69), as to whether agreement needed to be reached between the Bookmakers' Committee and spread betting bookmakers and betting exchanges (which he identified as a legal point.)"

56. In the light of concerns expressed by the Board about the lack of consultation, Mr Brack, chief executive of the Board, wrote on October 4 to Betfair, which had about 90% of the market at that time and to the Spread Betting Association enclosing some information about the Committee's recommendations and seeking their views so that he could brief the Board on the arguments which they may wish to advance. Betfair were sent only copies of the two recommendations set out in paragraph 29 above and part of the letter of 5 September, which includes the passages which I have set out in paragraph 25 above.

57. In its reply dated 5 October (3/143) (copied to all members of the Board), Betfair pointed out that there had been no formal consultation by the Committee with Betfair, that Betfair had not seen the Committee's submission to the Board and that therefore it could not comment on the submissions in their entirety and reserved the right to comment further "on those parts of the complete submissions that we have not yet seen." Betfair wrote that, "given the short time frame available",

Betfair had been unable to solicit the views of the other exchanges. In paragraph 7 Betfair referred to the rules of natural justice and procedural fairness and in paragraph 8 expressed concerns about "bias", given the makeup of the Board. In paragraph 12 Betfair complained of the failure on the part of the Committee to consult. In its conclusions Betfair submitted that the recommendations of the Committee should be rejected and that the Board should adopt the basis used in the 41st scheme.

58. The 10 page submissions made by Betfair were enclosed with the letter. On the first page of the submissions Betfair summarises its objections in the following way:

> "The justification given by the Bookmakers' Committee in the BC Submission appears to be that because the Bookmakers' Committee believes that betting exchanges may be squeezing the profit margins of conventional bookmakers and that betting exchanges generate less levy per pound of betting turnover, the basis on which betting exchanges are assessed must be extended. We explain:
>
> (1) why the Bookmakers' Committee's statistics and conclusions are insufficiently substantiated to be taken into account by the HBLB;
>
> (2) more importantly, why even if these statistics and conclusions were true, the conclusions are merely the effect of legitimate competition and, as such, constitute an improper justification for extending the basis of the charge; and
>
> (3) that the HBLB does not have the statutory authority to impose levy on anyone other than bookmakers and therefore the recommendation that "all betting exchange customers who wish to lay bets through … a betting exchange…should be charged a levy at a flat rate of 10% on any gross profits derived from laying bets on British horseracing" cannot be adopted.
>
> We oppose any decision by the HBLB to adopt a dual basis of assessment, given the questionable impartiality of the Bookmakers' Committee and the BHB, whose appointees represent about half of the HBLB, and the limited justifications put forward for the dual basis and the procedure employed in reaching this decision.
>
> We then set out the alternatives which we would submit are fair and therefore open to the HBLB. We conclude by recommending that the HBLB adopt a 42nd Levy Scheme in which betting exchanges continue to be charged, as is currently the case for the 41st Levy Scheme, on a commission basis. We indicate however that as a fair alternative, betting exchanges might be required to account for levy on the basis of their profitable layers' profits basis but that, if so, caps on liability should be imposed to protect against volatility."

59. Under the heading "Rebutting the various possible justifications for the BC Submission", Betfair summarised the Committee submission in the following way:

> "(1) The Bookmakers' Committee believes that the 41st Levy Scheme will generate £6m less levy than the Bookmakers' Committee initially predicted;
>
> (2) the Bookmakers' Committee believes that this shortfall is due (i) to profit margins of the conventional bookmakers being squeezed by "artificial" inflation of SP; and (ii) to the assumption that betting turnover channelled through betting exchanges generates less levy;

(3) therefore a new basis of levy should be imposed on betting exchanges."

60. Betfair submitted that:

> there was no convincing evidence that the profit margins of conventional bookmakers were down,
>
> if they were down that "may be for any number of reasons other than those cited",
>
> the original estimate of the expected levy was "an estimate based on a large number of assumptions any one of which may prove to be wrong as a result of factors unrelated to betting exchanges",
>
> the estimate may have been a deliberately optimistic estimate to procure a low rate of levy, "the betting exchanges present a convenient scapegoat on which to place the blame for the over-estimate", and that
>
> the estimate may prove to be wrong- "the betting exchange contribution alone was likely to be significantly in excess of the 1.3 million suggested by the Bookmakers' Committee."

61. Betfair submitted that betting exchanges do not generate significantly less levy per pound of betting turnover. They "have a significant incremental and multiplier effect on betting activity". They supported that submission with reasons.

62. Betfair submitted that there was no merit in the Committee's view that betting exchanges should pay more levy on the grounds that some on course bookmakers are choosing to hedge with betting exchanges. In the view of Betfair "betting exchanges are helping to deepen the market".

63. Betfair submitted that even if the profit margins of the conventional bookmakers were being squeezed by betting exchanges, "such effects are wholly irrelevant considerations for the determination of a new basis for charging levy on betting exchanges and cannot properly be taken into account by the HBLB in fulfilling its statutory duty." Betfair continued:

> "The conclusion of the BC Submission amounts to saying that any low margin bookmaker should be penalised and be required to pay more levy simply because they are low margin bookmakers. This would suggest that the Bookmakers' Committee are seeking to link liability to levy to turnover. We submit that one of the main reasons why the Secretary of State decided to shift the 41st Levy Scheme from a turnover-based system to a gross profits system was so that low margin operators would be encouraged and would not be prejudiced. The Bookmakers' Committee proposal would completely undermine the rationale behind this shift".

64. The submission continued:

> "Any decision to increase the charge paid by lower margin competitors is intrinsically anti-competitive, pandering to conventional bookmakers and encouraging them to sustain their oligopolistic overrounds and profit margins."

65. Betfair then submitted that the Board had no statutory authority to impose a levy on the layers setting out the arguments which I have already summarised above (paragraph 43).

66. Betfair continued:

> "Notwithstanding the statutory limitations, we believe that the logic of treating all layers equally regardless of whether or not they are registered bookmakers is completely flawed. Fundamentally the distinction between backing and laying on an exchange is arbitrary: if a punter offers odds on Man Utd not to win the Premiership, has he layed that outcome or backed the outcome Man Utd to win it? … Betting exchange users are generally ordinary punters who are prepared to enter a bet with other punters that an outcome will or will not occur. Unless a user is a registered bookmaker with all of the rights and obligations that entails (authority to advertise and solicit bets directly from the public, handle their stakes, pay out their winnings etc), there is no justification for treating him differently merely because he choose to bet that an event will not occur (i.e. 'laying') instead of choosing to bet that an event will occur (ie. 'back')."

67. Betfair then went on to deal with what they saw as the effect of the dual basis of assessment:

> "Betfair has calculated that if the dual basis of assessment proposed by the Bookmakers' Committee had been applied during the period April – September 2002, this would have generated liability to levy equal to approximately 19% of Betfair's commission over the same period.
>
> The new element in the BC Submission (i.e. 10% of all profitable layers' profits) would however generate an extremely volatile liability which would be impossible to predict. In many circumstances, levy liability will greatly exceed commission revenue generated by the betting exchange; indeed in any races where an odds on favourite loses, the levy liability generated will be many times greater than the commission revenue generated.
>
> This solution is also open to sabotage: Two people A and B could act in concert. Person A lays a horse to Person B for £10,000 at Evens and Person B lays that same horse to Person A, also for £10,000 at Evens. Regardless of the outcome, both Person A and Person B come out flat and thus pay no commission. However, if the horse fails to win then both Person A and Person B will have won on the "lay" part of their bets and will, together, generate £2,000 (£10,000 x 10% x 2) of levy liability for the exchange. Clearly, this is a grossly simplified example but it serves to illustrate how such a solution is very open to sabotage.
>
> The Bookmakers' Committee and the BHB may argue that it is up to the betting exchange whether it seeks to recover the cost from the layers themselves. It is quite clear however that that would not be a commercially viable option for the exchanges. There may be accounts which quite legitimately end up in the situation described above, where each is flat from a net winnings perspective but which would give rise to a large levy liability. Passing this cost on to layers would completely distort trading activity on betting exchanges. The exchanges would therefore have to choose between undermining the business model or paying the increased liability themselves. They would no doubt opt for the latter.
>
> In short, if the Bookmakers' Committee proposal is accepted, the liability of betting exchanges would probably be doubled and would be exposed to extraordinary volatility and sabotage. In such an oppressive environment, it is likely that some if not all betting exchanges will choose to relocate off-shore."

68. Betfair then set out why, in its submissions, it would be counterproductive if betting exchanges were forced off-shore.

69. In paragraph 5 Betfair set out what it said was the fair basis "which could properly be recommended to the Secretary of the State by the HBLB". That is, of course, an inaccurate statement of how the procedure operated.

70. Betfair went on to consider the second of the two recommendations of the Committee. The submissions explained that the exchanges resisted the "aggregated layers' profits basis" put forward by Customs and Excise because "of the volatility and unpredictability associated." Having stated that Customs and Excise had insisted upon this basis, Betfair went on:

> "The aggregated layers' profits basis has proved extremely volatile but appears to work reasonably well for short accounting periods, such as one month. However for longer accounting periods such as the one year period used for levy schemes, the aggregated layers' profits basis is unlikely to work well because over such extended periods the aggregated position of layers will tend to zero."

71. Betfair then referred to the Committee's recommendation that an "aggregated profitable layers' profits basis" be adopted. Having reiterated its previous objections, Betfair continued:

> "Also, as discussed above, this solution is flawed in practice in that it exposes the betting exchange operator to enormous volatility because the liability to levy is dependent not on the gross profits of its own operation but on those of its layers, which are not within its control. The aggregated profitable layers' profits basis would indeed be significantly more volatile than the aggregated layers' profits basis. It would also be open to sabotage. Despite these flaws, we believe it would be possible to accept the aggregated profitable layers' profits basis as fair as long as (i) it is the exclusive basis for assessing betting exchanges to levy; and (ii) sensible caps are placed on potential liability to ensure that it does not become unreasonably large and to manage the inherent volatility and potential for sabotage."

72. In its conclusion Betfair wrote:

> "We believe that this is best achieved by betting exchanges continuing to account for levy on a commission only basis. However if the HBLB prefers to adopt a profitable layers basis, we believe that this could be made fair if reasonable caps were imposed on liability to protect against volatility and sabotage."

73. On 16 October there was a meeting between the Chairman of the Board and representatives of the Committee. On the following day Mr Bartlett wrote a letter (3/160) to the Chairman of the Board stating that due to the concerns expressed in the letter and at the meeting:

> "… the Committee is now seeking legal advice in respect of its statutory remit in making recommendations which impact upon all bookmakers and bet-brokers; and also in respect of due process in discharging that remit."

74. In the light of the need to seek such advice, it was unlikely, so the letter stated, that the Committee would be in a position to submit recommendations for the next meeting of the Board on 23 October. No such recommendations were submitted and what normally would happen now had to happen, namely a meeting of the Board on the last day possible, 31 October, if a determination by the Secretary of State was to be avoided.

75. I turn to the account given by Mr Griffiths in his first witness statement of what happened in this period as far as he was concerned (1/75):

> "33. In and around 20 October 2002, I read an article in the Racing Post newspaper which stated that the Bookmakers' Committee had proposed that for the 42nd Levy Scheme, the levy imposed upon betting exchanges would be:
>
> (a) 10% of the commission received from bets on British horse racing; plus
>
> (b) 10% of the aggregate profitable layers' winnings bets on British horse racing (that is the total of only those betters who had placed bets in the period as layers and who, over the period, had made a profit from the bets they had laid – those who had made a loss would be excluded from the calculation).
>
> 34. Sporting Options never received any direct communication from the Levy Board or the Bookmakers' Committee regarding the proposals despite the facts that we were registered with the Levy Board, paid a Levy each month to the Levy Board and we were a betting exchange which, as the Levy Board and the Bookmakers' Committee must have known, had a real and immediate interest in any changes to the Levy Scheme as it applied to betting exchanges.
>
> 35. I was appalled that the Levy for betting exchanges could be set by reference to aggregate profitable layers' winnings. I was concerned that the proposal would have a very considerable harmful economic impact on our business in that we would have to pay a greatly increased amount in the Levy irrespective of the amount of income received.
>
> 36. I immediately telephoned Mr Rodney Brack, the Chief Executive of the Levy Board. He confirmed that the article in the Racing Post was correct. He expressed some sympathy with the position of Sporting Options. We arranged to meet a week later on 28 October 2002 to discuss the question of the levy proposed as it applied to us.
>
> 37. I also telephoned Mr Edward Wray, the Managing Director of Betfair. Mr Wray told me that he had received a letter early in October from the Levy Board setting out the proposals. I told him that I had received no such letter. He said that he had prepared a paper setting out Betfair's response to the proposals which he had submitted to the Bookmakers' Committee. He also told me that there was a meeting of the Bookmakers' Committee taking place the following Friday, 25 October 2002. I arranged with Mr Wray to attend that meeting with him.
>
> 38. I was very busy running Sporting Options at this time. In the short time available, I did not have the opportunity to prepare our case against the proposed Levy Scheme as thoroughly as I would have liked. It seemed to me the unfairness of the proposal was obvious and I proposed to put this to the Bookmakers' Committee on 25 October.
>
> 39. On 25 October 2002, I met with Mr Wray in a hotel some half an hour before the meeting with the Bookmakers' Committee was due to take place. He showed me a paper which Betfair had submitted to the Bookmakers' Committee. I reviewed this document quickly. I noted that it stated that Betfair preferred that the Levy for betting exchanges should continue to be assessed on the basis of gross commission but stated that it could accept that this Levy be assessed on

> the basis of aggregate profitable layers, provided there was a cap which meant that the amount payable did not exceed a percentage of gross commission. This did not seem sensible to me. Although such a cap would provide a degree of protection for betting exchanges, I considered that the only proper basis for assessing the Levy for betting exchanges was gross commission because it was imperative that the Levy was assessed proportionately to our gross profits (that is our commission) as it is for traditional bookmakers.
>
> 40. At the meeting, I made a number of points to the Committee. A copy of the minutes of the meeting was later provided to me... . During the meeting I made it clear that my view was that the only fair basis to assess the Levy on betting exchanges was (as with the 41st Levy Scheme) on gross commission received.
>
> 41. On the following Monday, 28 October 2002, I met with Mr Brack. He was extremely sympathetic to the position of Sporting Options and of betting exchanges generally. He agreed with all my points and he indicated that he thought that the only fair basis to assess the Levy for betting exchanges was on gross commission. After that meeting, I prepared a short note for submission to the Levy Board. I attach a copy at KRPG4 [3/204]."

76. The one-page note asked why betting exchanges should pay more than 10% of the commission, explained why, in the view of Mr Grifiths, betting exchanges had proved so popular, explained who used exchanges and offered help "to limit registered bookmakers using Exchanges in an undeclared private capacity".

77. According to Mr Brack in his witness statement (1/149):

> "What happened next was that I met with Mr Griffiths of Sporting Options on 28 October. Mr Griffiths had telephoned me (possibly on 20 October, although I am not sure) to express his concerns over the proposed 42nd levy scheme. Noting these, I had suggested that we meet. During this meeting, Mr Griffiths had explained why he was opposed to the Bookmakers' Committee's recommendations. He also set out why he disagreed with Betfair's attitude to these recommendations set out in Mr Wray's letter of 15 October 2002 (i.e. Mr Griffiths was only willing to accept the commission basis and was not prepared to accept the individual layers' basis, even with a cap). Contrary to what Mr Griffiths says at paragraph 41 of his witness statement, I did not express sympathy for the position of Sporting Options and the betting exchanges generally. Nor did I agree with the points he was making and indicate that the only fair basis to assess the levy for betting exchanges was on a gross commission basis."

78. It is not necessary for me to resolve the dispute as to what Mr Brack said. That is how Mr Griffiths understood what was being said. The existence of such a dispute is perhaps indicative of the kind of problems which can arise when important decisions are taken without a full opportunity for consultation being given.

79. For the 23 October meeting, Mr Brack prepared a paper (3/161), to which he attached the Betfair and Spread Betting Association replies to his letter of 4 October. Paragraphs 6-9 read:

> "On-course Bookmakers
>
> 6. Following members' comments at its September meeting, the Bookmakers' Committee has held further consultations with its members who represent the

> on-course bookmakers. This provided them with an opportunity to explain their objections to the Committee's recommendations in respect of on-course bookmakers. It is understood that, as a result of those consultations, amendments will be made to the Committee's recommendations, but this will not be in time for their consideration at the 23rd October meeting.
>
> Legal Advice
>
> 7. In view of the comments expressed at the last meeting by the Chairman of the Tote with regard to the Committee's recommendations in respect of betting exchanges and spread betting companies, legal advice was sought from the Board's solicitors, Herbert Smith, on the process which the Committees had followed. A copy of Herbert Smith's advice is attached as Appendix 'B'.
>
> Submission from Betting Exchanges and Spread Betting Companies
>
> 8. In the light of Herbert Smith's advice, the Chief Executive held meetings with representatives of Betfair, the largest betting exchange company, and the Spread Betting Association. Both groups, at their respective meetings, made it clear that;
>
> (a) they were not represented on the Bookmakers' Committee;
>
> (b) they had not been properly consulted, in their view, by the Bookmakers' Committee in the preparation of it s recommendations; and
>
> (c) they objected strongly to the recommendations on the grounds of quantum.
>
> 9. As a result, they were invited to make written submissions to the Board setting out their views. …"

80. The Board did discuss the 42nd Scheme at the 23 October meeting (3/166), but, in the absence of amended recommendations from the Committee, could not resolve the issue of the Levy. The Chairman noted that any recommendations imposed on the spread betting and betting exchange companies "may be open to legal challenge".

81. Mr Bartlett told the meeting that agreement had been reached with the on-course bookmakers, that the Committee intended to have a consultation process with the spread betting and betting exchange companies and "he was confident that there would be a deal for settlement." (The words "for settlement" were added in by way of amendment at Mr Bartlett's suggestion at the 31 October meeting, 3/226). In so far as the OFT were concerned, following consultations with the OFT, the amended recommendations would not be conditional (see paragraph 36 above and see also the 30 October recommendations 3/213, in which the paragraph regarding the OFT was omitted).

82. Mr Bartlett commented:

> "that, in his view, there was a changing betting marketplace, and a lack of a clear understanding of what the betting exchange business entailed prevented the establishment of a fair and level playing field for all interested parties."

83. During the meeting Mr Bartlett agreed with the views of Mr Brown that, if there was a referral, it was highly likely that the Secretary of State would merely repeat her determination of the relevant terms of the 41st Levy Scheme. Absent any agreement, the Secretary of State was likely, in the

view of Mr Bartlett and Mr Brown, to adopt the 10% of the gross commission basis for determining the levy for the betting exchanges and not the basis which the Committee were seeking. Mr Brown, Chairman of the Racecourse Association Limited, made that point strongly in a letter dated 28 October to Mr Hughes (3/187), to which I shall refer shortly.

84. The minutes also record the following:

> "MR JONES suggested that in the event there was no agreement reached with the betting exchanges and spread betting companies, there should be acceptance of no change to the levy rates by the Committee. He proposed that this would provide time while the BHB pursued its commercial agreement. He felt that if higher rates were forced through they would attract a legal challenge. This could lead to unpleasant public allegations of collusion between the BHB and the bookmakers for anti-competitive purposes.
>
> Taking members' views into account, and his understanding of the situation, Mr K BROWN said that if it was being suggested that there was a difference between the two sides of perhaps an additional £3m, this amount was not so significant to pursue that it should result in a referral to the Secretary of State, who had already made it clear that she would not wish to entertain another levy scheme determination. He also said that, if there was a referral, it was highly likely that the Secretary of State would merely repeat her determination of the relevant terms of the Forty-First Levy Scheme. He said that in risk: reward terms, in his view, to risk the whole levy against an extra £2m-3m was unjustified. Also, the fall out from any referral would be high and the reward very little; it must be avoided at all costs. A compromise was necessary and it should be agreed next week. THE CHAIRMAN AGREED.
>
> MR BARTLETT said that he supported MR K BROWN'S views regarding the fallout of any referral, and his Committee were working hard to avoid this. However, in terms of the amount of money that the betting exchanges should pay, he pointed out that they earned 90% of their business from British horseracing using the BHB's racing data. Whilst the exchanges had offered to pay levy, it should be acknowledged that their businesses were successfully operating as a result of a tax concession but once this was removed their businesses would founder. MR BARTLETT said the betting exchanges should pay the same as other bookmaking businesses. MR RICKETTS commented that the BHB was not holding the Committee to its commercial intentions."

85. I turn briefly to the meeting on October 24 between the Chairman and three members of the Committee, Mr Griffiths, and representatives from Betdaq (another exchange) and Betfair, including Mr Wray (3/173). Before the meeting Mr Wray of Betfair had asked, amongst other things, what was the basis of the meeting and asked whether the exchanges would be notified in time of the decision of the Committee in time to make further submissions (3/147). In answer to the latter enquiry, Mr Bartlett said, at the beginning of the meeting, that they would not be notified by the Committee, "but it would be a matter for the Board if it chose to share the contents with others". Neither the minutes of the 2½ hour meeting, nor any written summary thereof, were made available to the Board. The minutes are therefore of limited relevance in this case. Mr Bartlett did say that betting exchanges should apply to the Secretary of State for representation on the Committee, "noting that it had taken the BBOA some years of lobbying to acquire the two seats they currently held". During the course of argument before me, Mr Pannick, justifying his submission that there was no obligation upon the Board to consult, submitted that, if they wished to be consulted, the betting exchanges should apply for membership of the Committee. Not only is that argument unattractive, it also has the flavour of "catch 22", given what Mr Bartlett was saying at this meeting.

86. The minutes show, amongst other things, that Mr Williams of Betfair protested that "the Committee had made its case for the proposed charging structure based on a need to address a perceived shortfall in the current levy and was now seeking to change its approach to one of equitable charging". As will be shown later, Mr Williams was right to note that the Committee was seeking to justify the change by reference to equity, but was, it appears, wrong to think that the original justification was to be abandoned (see paragraph 93 below).

87. Mr Ross, who attended the 31 October meeting of the Board as a Committee observer, said that he interpreted the Betfair letter as saying that the exchanges were willing to pay levy as a percentage of their commission or as a percentage of their layers' earnings, but not both. Mr Wray made it clear that, if the latter route was followed, the method of assessing the levy would have to include safeguards against volatility and sabotage (3/176). Mr Ross repeated the same or similar assertion on other occasions (3/177,179,182).

88. Betfair made it clear that the current basis was their preferred option and that it "was the fairest basis for charging the levy". If the Committee's second recommendation was to be adopted, there would have to be a cap because of sabotage and volatility, which it was said should be at 10%. Mr Griffiths said that "… commission was the sole revenue stream for betting exchanges and that levy should therefore be payable on that alone."

89. On 25 October the Chief Executive of another betting exchange company, BackAndLay, wrote an email (3/185-186) to Mr Brack strongly attacking Betfair and the Committee's proposals. Mr Brack understood that BackAndLay were expecting (wrongly it turned out) to start trading in late 2002 (see email of 10/06/2003 following the hearing). An edited version was published by Racing Post on 31 October- which Mr Brack believes that all members of the Board read. According to Mr Brack: "I believe that all board members were already aware by 25 October of the difference between what Mr Davies describes as the 'layers' aggregated profits basis' and what he describes as the 'layers' profits mechanism' apparently adopted by the BHB." "I would be very surprised" if they did not read the Racing Post that day including this letter" (ibid.). The email was not forwarded to the Board members although Mr Brack believes that he would have discussed it with the Chairman. The email reads:

> "Richard Wright's article (Racing Post 25/12/2002) illustrates the twin folly of Betfair's claims it is not a bookmaker and Betfair's dubious deal to pay Gross Profits Tax on exchange 'layers aggregated profits' which, as I predicted in a letter published here earlier this year, is now beginning to backfire on them, leaving their users and other exchanges caught in the crossfire.
>
> Betfair and Flutter (now part of Betfair) negotiated this deal with the government, fully aware the low over-round books and professional backers in operation on their exchanges were ensuring the layers collectively lost and there would be little GPT for Betfair and Flutter to pay [see further Betfair submissions, paragraph 70 above].
>
> But GPT for betting exchanges is under review now and, more immediately, the BHB has adopted the 'layers' profits' mechanism as the basis for paying for the Data Rights Licence, but has cunningly amended it so one layers' losses cannot be offset against another.
>
> Moreover now, capitalising on Betfair's dogmatic insistence it is not a bookmaker, the BHB is set to impose a second licence, levying 10% of the exchange's gross commissions on UK horseracing, in addition to 10% of layers' profits on UK horseracing.

The 10% levy of all commissions on UK horseracing is reasonable, but an additional 10% of all layers' profits could leave exchanges with the twin consistently exceeding revenues, raising the spectre of the exchange having to pass the Levy onto its users in the form of higher commission rates.

The saddest aspect of this shambolic performance by Betfair – which leaves themselves, other exchanges and all exchange users in a parlous state – is that it could so easily have been avoided.

Exchanges are bookmakers.

Bookmaking is about laying bets to lock in a profit on any given event so that, ultimately, the bookmaker has no interest in the outcome of the event.

By locking in a profit on every matched bet (via the commission) exchanges demonstrate that "bet brokering" is actually bookmaking in its purest form.

'Layers' on exchanges are NOT bookmakers.

They are punters, betting on thing not happening, the same as people who sell performances with spread firms are punters.

Bookmakers want a level playing field – fair enough.

But these new proposals are not equitable.

Bookmakers make their Gross Profits via their over-rounds, exchanges make their Gross Profits via gross commission.

The fact exchanges garner less in commission on turnover than bookmakers do via the over-round is a key reason why exchange betting is a superior product for "win only" and "place only" betting to betting with a bookie in the modern era.

It's not creating a level playing field to penalise an exchange because it offers better value for a punter's betting pound than a bookmaker.

That would be like Harrods saying Asda should pay more higher rates of tax because Asda charge their customers lower prices and are nicking Harrods' customers.

Exchanges should pay 15% GPT on all its commissions to the Treasury and an additional 10% of its UK horseracing revenues to the BHB in Levy."

90. On 28 October Mr Keith Brown wrote a letter to Mr Hughes stating that he would not be able to attend the meeting on 31 October (3/187). The letter, copied to Mr Tristram Ricketts, another member of the Board, stated:

"However, I would like to reiterate my position elucidated at the last meeting. It would be disastrous for Levy and racing for this to be referred to the DCMS. It sends out totally the wrong message that we cannot manage our own affairs and should have sorted out the commercial arrangements months ago. There must, therefore, be a strong possibility that the DCMS would first roll over the 2002/3

> settlement if they received a referral. However, a Chancellor anxious for revenue would see a rise in the GPT rate fair game and even a punishment to the bookmakers. Therefore a referral can only be to everybody's disadvantage.
>
> We cannot run the risk of legal action from the bet-exchanges for potentially another £2m of income and risk £85-90m from the Levy. I fully understand that the bookmakers see bet-exchange operations in an uneven playing field, but it may not be as uneven as they make it out to be. The Levy is not there for commercial advantage. Furthermore it is clear that current legislation was framed at a time when this type of technological innovation could never have been envisaged. The Minister seemed clear that he wished to avoid a conflict today but would legislate tomorrow. The Bookmaker Committee and the Levy Board must be careful not to pre-empt legislation. The DCMS made its views known on the Levy to be paid by bet-exchanges and spread betting companies at the last settlement and the lowest risk strategy is to continue with the existing rates until a firm commercial agreement is put in place.
>
> I hope you will be able to persuade the Bookmaker Committee that a referral is in the interests of neither the bookmakers nor the HBLB."

The letter was not, it appears, included within the papers for the meeting of 31 October.

91. By now a Board meeting on 31 October was inevitable, given that there had been no new recommendations before the 23 October meeting of the Board and given that the Committee was meeting only on the afternoon of the 30 October.

92. On 30 October starting at 2.00pm the Committee agreed upon what it described as its "Final Recommendations". In the words of Group Captain Nixon:

> "As a matter of longstanding practice, a committee agrees its final recommendations at the end of the day on 30 October, leaving me, as Secretary, little if any time to turn around the necessary documents and forward them to the Levy Board in time for their meeting on 31 October."

The minutes of that meeting, heavily redacted to exclude legal advice, appear in the documents prepared for this hearing (2/161) although they did not form part of the material upon which the Board reached its conclusions on the next day.

93. The letter accompanying the final recommendations described the new proposal regarding betting exchanges as "fair and equitable", but did not abandon the original justifications for change. The final recommendations contained some changes to the original recommendations. Whereas the justification for the proposed changes for the betting exchanges set out in the September recommendations (paragraphs 29 and 34 above) had referred to the "individual liability" of a person laying a bet on a betting exchange, the reference to individual liability was removed. The relevant part of paragraph 6 now read instead:

> "On reflection, we believe this basis [the 41st Scheme basis] to be inappropriate because the exchanges themselves do not bet on race outcomes, <u>whereas, like bookmakers, those who offer to lay horses through the medium of the exchanges do</u>. We therefore consider that a more suitable mechanism would be for the exchanges, as the sole facilitators of such betting, to be accountable for a levy assessed on the gross profits of their successful layers; and we will make recommendations to this effect." (Emphasis added)

The paragraph setting out the proposals for betting exchanges was also altered. In the September proposals (paragraph 29 above), there had been one paragraph for betting exchanges and a separate paragraph for betting exchange customers. The new single paragraph started with these words:

> "We recommend that betting exchanges should be assessed for levy on the basis of the gross profits earned by those of their customers who successfully lay bets on British horseracing through the medium of a betting exchange."

The proposed method of method of calculation is described in terms similar to those used in the September recommendations. The Committee was now basing its case for change upon the basis that layers on an exchange were like bookmakers, and should therefore be treated, for levy purposes, in the same way whether they were permit holding bookmakers or not. In September the Committee was recommending that the betting exchanges be responsible "for carrying out the required calculations and making the appropriate payments" (see paragraph 29 above). Under these recommendations, exchanges, "as the sole facilitators of such betting" were to be accountable for a levy assessed on the gross profits of their successful layers.

94. From the new recommendations, the committee excluded the recommendation that the betting exchanges should pay 10% of their gross profit by way of levy. These recommendations also dealt with the issue of double counting (see paragraph 31 and following above) in the following way:

> "Furthermore, we recognise that, under the provisions of the 41st Scheme, permit holding bookmakers are required for levy purposes to declare any gross profits accrued as a result of conducting business through the exchanges. We therefore recommend that, if the exchanges are responsible for making the appropriate levy payments, irrespective of whether or not they choose to charge this cost to their customers, the liability should be disregarded as discharged in full and that the requirement for permit holders to make separate declarations in respect of levy should be discontinued." (Emphasis added)

95. Alterations were also made to the figures for the estimated yield (see paragraph 47 above). Whereas in the September recommendations, the estimated yield had been in the order of £94.31 million to which "may be added an allowance of up to £3.5M for receipts from racecourse bookmakers, betting exchanges and their customers", the Committee wrote that it "estimates the projected yield from the 42nd Scheme from all sources to be in the order of £98 million." There was no reference in the final October 30 recommendations (as opposed to the draft, 3/349) to likely receipts from the betting exchanges under the proposed levy scheme. The Committee went on to state its belief, as it had done in the September recommendations, that the effect of the betting exchanges had been to reduce the margins of bookmakers. The Committee also repeated its view that, if this trend continued, "we would estimate the levy yield to be in the region of £93M - £94M."

96. The members of the Board were provided with a very brief paper (3/189) from Mr Brack. In his paper there was no reference to the views of the betting exchanges, of Mr Griffiths or of the Spread betting Association and no analysis of the competing arguments for and against adopting any recommendation which the Committee had made in September or might make now. That is understandable if, for no other reason, he did not know what recommendations the Committee would make when he prepared his report. Presumably Mr Brack learnt what the new recommendations contained some time late on 30 October. It is not apparent when the Board members learnt about the new recommendations, perhaps only when they arrived for the 11.00am meeting on the next day.

97. The only document given to the Board members at this meeting was a 12 page detailed report from Europe Economics to which I shall briefly refer later, the letter from the Chairman of the Committee dated 30 October (3/206) and the "Final Recommendations" (3/344). The only other documents, relevant to this case, which the members would have had were the documents made available at the 23 October meeting, namely the Betfair and Spread Betting Association submissions appended to the 23 October Board meeting papers.

98. The Board members had nothing in writing which reflected the views of the betting exchanges at the October 24 meeting with the Committee or any conclusions of that meeting, the Committee having deleted from the draft letter of 30 October prepared by Group Captain Nixon the short passages in which the position of the exchanges as at 30 October were summarised. Nor did the Board have a written note of the views of Mr Griffiths expressed at his meeting with Mr Brack on 28 October. Mr Brack in his witness statement describes his actions after the meeting:

> "I therefore gave an oral report of the meeting to the Chairman and the independent members of the HBLB, shortly after the meeting (and certainly before the next board meeting on 31 October 2002)."

99. That is in part confirmed by Mr Hughes in his witness statement, who writes:

> "Sporting Options' insistence on a commission-based levy had been communicated to me and to the two independent members at a briefing with Mr Brack who had met with a representative of Sporting Options."

100. There is no evidence that the points made by Mr Griffiths were transmitted to other members of the Board. I return later to a witness statement made by Mr Hughes and dated 4 June (the second day of the hearing).

101. At the meeting in addition to Mr Bartlett as a voting member, another member of the Committee, Mr Ross, attended as an observer, as he had before.

102. I set out the minutes (3/222) almost in full, the contents of which were closely examined during the course of the hearing. Apart from a small item, the only matter discussed during the meeting was the 42nd scheme. I omit the content of the discussions relating to the issue of the percentage of gross profit used by the Board to identify how much of the betting business carried on by a traditional bookmaker relates to British horseracing, if he is unable to identify the precise proportion (3/161). In September Europe Economics had been appointed by the Board to analyse the data relied upon by the Committee to support its recommendation in September that the appropriate figure was 55%.

103. The minutes relating to the first very short part of the meeting read as follows:

> "Noting the tabled proposals, as amended, from the Chairman of the Bookmakers' Committee set out in a letter dated 30th October 2002, THE CHAIRMAN asked if copies had been sent to the betting exchanges and spread betting companies; he was of the view that this should occur. MR BARTLETT said that this had not occurred and that he wished to reflect on the request. MR JONES agreed that sending the amended proposals to the affected parties, as soon as possible, would be appropriate."

104. Mr Bartlett and Mr Ross left the meeting to discuss the question whether copies should be sent to the betting exchanges and spread betting companies, with the Committee, the members of which were present in the building. On their return at 11.10am, the Board was told that the Committee took the view that it was inappropriate to distribute the proposals because it would "interrupt the

negotiating process between the Committee and the Board to no good effect" and by "re-opening the negotiations with the … betting exchanges and spread betting companies, it could negate the consensus achieved with considerable difficulty, by the Committee." The minutes read:

> "He suggested, however, that the Board members could decide if they wished to distribute the information to the two parties."

105. It will be remembered that Mr Bartlett had said at the October 25 meeting, in answer to the question whether the exchanges would be notified in time of the decision of the Committee in time to make further submissions, that "it would be a matter for the Board if it chose to share the contents with others". The minutes show that Sir Eric Parker of the BHB said "that he was not convinced that such distribution by either side would serve any purpose; he believed it would be counter-productive to the process". The minutes record Mr Bartlett as saying "that the Committee had considered long and hard during the previous day on how to achieve a level playing field that was deemed fair for all affected parties".

106. The minutes continue:

> "Comments then ensued between MR JONES, MR BARTLETT, THE CHAIRMAN and MR ELLIOT on the effect of not circulating the proposals in the event that the two parties chose to seek a Judicial Review. It was confirmed that the exchanges and spread betting companies were not aware of the detail of the Committee's amended proposals.
>
> MR ROSS [the observer] said that the Committee had carried out its statutory responsibilities by circulating its final, amended proposals to the Levy Board. It was his view, therefore, that it was not necessary for the exchanges and spread betting companies to be accorded the right to view and comment on the amended proposals. THE CHAIRMAN reiterated his view, and agreed with MR JONES and MR ELLIOT that the proposals should be circulated by the Committee to the two parties as a matter of courtesy. SIR ERIC agreed that if the proposals were to be circulated, it was for the Committee and not the Board to do this.
>
> In response to MR BRACK, MR BARTLETT said that the Committee's secretary had visited and consulted with the two parties in July [apparently Betfair, but see paragraph 58 above, and the Spread Betting Association] before the initial recommendations were prepared. He confirmed that the Committee had taken legal advice to the effect that the Committee should consult further on the recommendations with the exchanges and spread betting companies; this had been done and, as a result, the proposals had been amended.
>
> Following further comments from THE CHAIRMAN and MR BARTLETT, MR JONES proposed that, in the absence of the Bookmakers' Committee being prepared to send their proposals to those parties materially affected by the proposals, the Board should do so. SIR ERIC proposed, in amendment, that the Board should request the Committee to send them to the two parties not represented on the Committee. The Board then voted on the amendment and it was carried. Upon being put as the substantive motion,
>
> THE BOARD
>
> RESOLVED:

> That the Board should request the Committee to send its amended proposals to the two parties not represented on the Committee."

107. The Board thus left it to the Committee to decide whether to send the proposals, presumably in their entirety, to the two parties concerned. As will be shown shortly, the Committee in fact declined to do. Thus the new proposals were never sent to the betting exchanges or the spread betting companies for their views. The Board's position on this matter was consistent with the position taken by Mr Pannick at the hearing, namely that there was no obligation on the Board to consult.

108. The discussion then turned to the spread betting companies, the Chairman expressing concern about the fact that the Committee had not revised its proposals. The minutes read:

> "THE CHAIRMAN then thanked the Committee for its amended proposals, but expressed concern regarding the lack of change in the proposals affecting the spread betting companies. He said that the proposed levy rate of 10% represented a 400% increase over the Secretary of State's determination in March of 2%. He understood the Committee's desire to set a level playing field between competing bookmakers and that it was consistent with the other proposals. However, it could make the Board vulnerable, if it was accepted on the proposed basis."

109. Following a discussion about horseracing's share of total gross profits, the meeting addressed the issue of the betting exchanges. The first issue was the projected yield from the amended proposal:

> "Both MR JONES and MR ELLIOT requested clarification on what the amended proposal relating to the payment by betting exchanges would yield compared to the initial proposal. MR BARTLETT and MR SMITH confirmed that this was a difficult calculation and not easy to estimate because of the fast changing nature of the betting exchanges' business. SIR JOHN also expressed surprise that this was not available, and added that even an educated guess would be helpful. MR ELLIOT accepted that the proposal would increase Levy Board income."

110. Mr Elliott, an independent member, "stressed that, in his opinion, the real logic behind" the proposals regarding betting exchanges "was to protect the profits of the bookmakers from a new entrant to the market, with the BHB having a financial incentive to support them." That was a reference to the policy adopted by the Board to use the 10% of gross profits as a basis for determining the licence fee which bookmakers had to pay to use the data about races (paragraph 36 above). The Chairman said that he "understood that the Committee's proposals reflected the BHB's commercial licensing deals in areas where these had been agreed." In fact they also represented the policy underlying the contractual negotiations with the betting exchanges and spread betting companies.

111. Mr Smith (BHB), attending in the place of Mr Keith Brown, then asked "if yield was more important than equity". The minutes read:

> "Commenting on the levy, its statutory process, and having regard to the fair treatment of all parties to the agreement, MR SMITH asked if yield was more important than equity."

112. The Chairman said "that there was no reference in the statutory arrangements to equity."

113. Mr Brack then noted that the established criteria in agreeing a levy were to take into consideration the needs of racing and the capacity of bookmakers to pay.

114. Mr Ricketts asked, in relation to the change to the recommendations regarding the betting exchanges, whether the betting exchanges had argued that they did not have the capacity to pay. That question, according to the minutes, led to an answer by Mr Bartlett upon which the claimant relies heavily. According to the minutes:

> "MR BARTLETT confirmed that the betting exchanges were willing to pay either on an assessment of the profits of their successful layers, or on their gross commissions, but not on both."

115. If that represents accurately and fully what Mr Bartlett said in answer to the question posed by Mr Ricketts, then the members were not being given an accurate account of the discussions on October 24, discussions which had followed the Betfair submission of October 5 and of which the members had a copy. The claimant, as Mr Bartlett knew, was not willing to pay on an assessment of profits basis and Betfair were only willing to pay on such a basis if a cap of 10% was in place to avoid volatility and sabotage. The position of both had been made very clear at the October 25 meeting in answer, particularly, to comments made by Mr Ross (see paragraph 87 above). Miss Rose points out the similarity between what Mr Bartlett is recorded as saying and that which Mr Ross is recorded as having said at the 25 October meeting. BackAndLay (paragraph 89) were in a similar position to the claimant.

116. The minutes continue:

> "He [Mr Bartlett] also explained the Secretary of State, when determining the Forty-First Levy Scheme, had had available to her a Nottingham Trent University Report commissioned by the Spread Betting Companies themselves. MR BARTLETT said that at that time the Report was not passed to the Committee, so the Committee was unable to express a view on whether what was proposed [by the Secretary of State] was fair or equitable. In fact, a request for the same Report the previous day had been refused. This had not been helpful to the current process."

117. Mr Jones said that he believed that the Committee was attempting to align the payment by betting exchanges with the payment by bookmakers. The Chairman said: "that it was important not to double guess the Committee's motivation". Mr Jones in this part of the discussion appears to be referring to the Committee's view that layers on an exchange were bookmakers and should therefore be treated, for levy purposes, in the same way as permit holding bookmakers (se paragraph 93 above). If so, the Chairman's reply is not easy to understand. The rationale for the proposed change was obviously an important, if not vital, matter to take into account.

118. The Chairman continued: "with no representation on the Bookmakers' Committee that was why it was important to circulate the Committee's proposals to the involved parties." Once again the Chairman is expressing the view that the proposals should be circulated to the "involved parties" because of the absence of representation on the Committee.

119. The minutes then record:

> "Both MR JONES and THE CHAIRMAN agreed that betting exchanges were a new and largely 'unknown' element to the betting industry and, therefore, it was necessary to receive a robust proposal from the Committee."

120. The minutes then include the following passage upon which the claimant also relies heavily:

> "In response to SIR ERIC, MR BARTLETT confirmed that the Committee's proposal relative to the betting exchanges was different only in detail to the arrangements with Customs & Excise, however, this was currently under review." (Emphasis added)

121. If that is what was said, it is wrong. They did not differ "in detail", as I shall show below (paragraph 187). The basis being proposed was the "aggregated profitable layers basis". That contrasts with the "aggregated layers basis", in which the accounts of all layers with the exchange are aggregated over the levy period, whether profitable or not. The aggregated layers basis was the basis then used by the Customs and Excise to assess the gross profits tax on betting (see paragraph 30 above). I have already rehearsed the views of Betfair about the risks of volatility and sabotage if the aggregated profitable layers basis were to be adopted without a cap.

122. Neither of the two passages upon which the claimant relies heavily were corrected when the minutes were considered at the next meeting. Mr Bartlett suggested an amendment to the paragraph following the passage set out in paragraph 113 above, which amendment was accepted.

123. The minutes continue:

> "THE CHAIRMAN then summarised the discussions:
>
> It was clear that members still had concerns on several aspects of the amended proposals and they could not be agreed as they stood;
>
> Regarding spread betting companies, the consensus was that there appeared to be concern about the sensitivity of increasing their payment level to the proposed proportion;
>
> It was acknowledged that the Committee had gone through the proper consultation process in finalising the proposal relative to betting exchanges, which was deemed fair and in line with the needs of racing; however, noting earlier comments, he urged the Committee to consider circulating the proposal to the betting exchanges"

124. Although Miss Rose sought to interpret the last passage as showing that a decided view in favour of the proposal regarding betting exchanges had by now been reached, a look at all the minutes shows, as Mr Pannick submitted, that this cannot have been the position at this point in time. Indeed why ask the Committee again to circulate the proposals?

125. The minutes continue:

> "The Board felt that the bookmakers should simply declare their gross profits on British horseracing, and there should not be a zero rated category based on foreign horseracing;
>
> There was discontent regarding the 54% default level set for British horseracing's share of total gross profits.
>
> In requesting the Committee's members to reflect on the comments that had been made, THE CHAIRMAN proposed that the meeting be adjourned until 2:00 pm so that amendments to the recommendations could be made; he proposed that a Vote on the Committee's then proposals should take place at that time.

The meeting adjourned at 12.20 pm and reconvened at 2.00pm."

126. When the meeting reconvened, the Chairman said that that the Board had (presumably during the adjournment) again asked the Committee to forward the amended proposals to the betting exchanges and spread betting companies. Mr Bartlett reported that his colleagues on the Committee had agreed that the "circulation of the amended proposals would not be done". "[I]t was the Committee's belief that it would fetter their ability to further discuss levy proposals with the Board". This was noted by the Board.

127. A letter from the Spread Betting Association was tabled. It alleged procedural failures by the Committee vis-à-vis the spread betting firms.

128. The amended recommendations from the Committee were then subject to a vote- seven members voted against and only Mr Bartlett in favour.

129. After discussion about the 55% default figure, the discussions turned again to the position of the spread betting companies and the betting exchanges. The minutes read:

> "THE CHAIRMAN said that the independent members retained concerns about the proposals in so far as they related to the spread betting companies. He wished to invite the Committee to consider rolling forward the terms of the Forty-First Levy Scheme. This would provide time for the Committee to study the position of the spread betting companies before making proposals for the Forty–Third-Levy Scheme. He said that this was not intended as a criticism. In response to MR BARLETT as to why the on-course bookmakers were not included in this request, THE CHAIRMAN said that they were represented on the Committee and had demonstrated their collective responsibility in endorsing the majority view of the Committee. It was felt that the possibility of a legal challenge from the on-course bookmakers was minimal. MR BARTLETT did not agree with that view. MR ELLIOTT said that the NAB (on-course bookmakers) had been make privy to the Committee's proposals, whereas the betting exchanges and spread betting companies had not; this was the key point of difference. MR BARTLETT explained that the two parties had in fact received the first set of proposals presented in September."

130. This was a reference to the Board's letter to Betfair and the Spread Betting Association in early October and does not, it appears, accurately reflect the fact that only the part of the proposals which affected them had been sent. The minutes continue:

> "On behalf of the independent members, THE CHAIRMAN urged the Committee again to consider rolling forward the relevant terms of the Forty-First Levy Scheme arrangements. He added that, if there was a referral to DCMS, it was likely that this would be the basis of the Secretary of State's determination."

131. Thus, at this stage, the Chairman, on behalf of himself and the independent members, was urging a vote for the position adopted for the year before by the Secretary of State. Mr Jones then expressed his support for the independent members' views, but was open to persuasion on the 58% vs. 55% issue (the latter being sought by the Committee).

132. Unlike the independent members, the BHB representatives confirmed that they were content with the proposals relative to the betting exchanges and the spread betting companies. It was their belief too that the risks of a legal challenge in adopting them were minimal. They were inclined to support the proposals.

133. The Chairman then said that if the Committee wished to make any further amended recommendations in the light of the comments that had been made, he would propose reassembling at 3.30pm.

134. The meeting adjourned at 2.20 pm and reconvened at 3.30 pm. The Board was then told by Mr Bartlett that he had briefed his colleagues on members' comments. He told the Board that:

> "The consensus was that the Committee had prepared a fair submission for the Board's consideration; this was based on the premise that there was no discrimination, and all the betting media were treated equally."

He said that, in the Committee's view, "the threat of a Judicial Review was not a factor they wished to consider". He confirmed that there was no change in the 55% vs. 58% issue.

135. The meeting adjourned at 3.35 pm. There was thus "stale mate". If put to a vote, the October 30 proposals would not be approved by four members of the Board, with the consequence that the Secretary of State would have to determine the levy.

136. During the next two hours, the Committee met and revised its recommendations. In the new letter (3/214) the Committee made it clear that it would make no new recommendations in respect of betting exchanges and that it was their belief that the recommendations were fair and reasonable. In so far as the spread betting firms were concerned the Committee stated that it remained committed to the principle that all bookmakers should pay the same 10 per cent of gross profits on UK horse racing. The letter continued:

> "However, we accept that more research may be required in pursuit of this objective and are therefore prepared to recommend that, for the period of the 42nd Levy only, the rate of 2 per cent gross profit determined by the Secretary of State for the 41st Scheme should remain in place. … [W]e do not accept that 2% is a fair rate when compared to other bookmakers."

137. As to quantum, the minutes summarise the contents of the letter:

> "The Committee had taken note of members' comments, and the BHB's in particular, and were prepared to recommend a British horseracing default figure, increased to 57%, from 55%, for the Forty-Second Levy Scheme."

138. The revised recommendations (3/216) included the same figures for "Estimated Yield" (3/221) as had been included in the letter of the day before (see paragraph 95 above) with again no figure for any projected yield from the betting exchanges .

139. By adopting the revised scheme, the Committee was giving way on the spread betting companies, accepting a default figure of 57% rather than the 58% which members of the Board had been seeking and the 55% which the Committee had been seeking, but refusing to alter its position on the betting exchanges.

140. The meeting reconvened at 5.25. The minutes show that the new proposals were outlined by Mr Bartlett. Any discussions about the 57% figure and about the betting exchanges are not recorded in the minutes. When the revised scheme was put to the vote at about 6.30 pm the Chairman proposed, and on being put to a vote, the Board resolved, by six votes to two (Messrs Jones and Elliott dissenting) that the final recommendations for the terms of the Forty-Second-Levy Scheme, 2003/04, as presented by the Bookmakers' Committee, be approved. What caused the Chairman and Sir John Robb apparently to change their minds is not revealed in the minutes.

141. The minutes then read:

> "THE CHAIRMAN expressed the Board's appreciation to MR BARTLETT and MR ROSS for the efforts that they and their Committee colleagues had made in proposing acceptable terms. MR RICKETTS, on behalf of the BHB representatives, endorsed the CHAIRMAN'S comments.
>
> He noted that there were likely to be a number of variations between the levy agreement and the commercial deal that would ultimately be concluded. He expressed the hope that the BHB's support today would not prejudice any future talks to come."

An overview of the events leading up to the vote at 6.30

142. I have no doubt that the manner in which the 42nd Scheme was determined is far from satisfactory. In accordance with what appears to be the normal (and in my view regrettable) practice, the Board's decision was made at almost the last possible moment with the knowledge that if the Committee's revised recommendations were not accepted, the decision would have to be made by the Minister- something which, from the outset, was not thought to be desirable and which would have resulted, so it was thought, in the rolling over of the 41st scheme.

143. The revised proposals from the Committee only reached the members of the Board on 30 or 31 October. The further final revisions were only presented to the Board late in the afternoon of 31 October, with only some six and a half hours to go before the deadline. The betting exchanges "lost out" at the last moment when the Chairman and Sir John Robb apparently changed their minds, faced with a refusal by the Committee to recommend that the basis for assessing the levy under the 41st scheme should continue in so far as the betting exchanges were concerned. If they had not changed their minds, so it appears, the decision would have to have been made by the Minister.

144. There was no report from Mr Brack summarising the complex competing arguments, as one might expect for a decision of this kind. Indeed there could not have been such a report given that the Committee decided not to meet until the afternoon of 30 October to produce its further recommendations.

145. Contrary to the wishes of the Board, as expressed at the start of the meeting, in a vote during the morning of 31 October and reiterated at the conclusion of the morning meeting and during the mid-day adjournment, no opportunity was given to the betting exchanges to see and comment on the revised proposals of 30 October. Indeed the betting exchanges had never even seen the full September recommendations. The Board was not provided with minutes of the consultation that did take place between the Committee and the betting exchanges on 25 October nor were all members of the Board provided with the views of the claimant and BackandLay as expressed to Mr Brack. Indeed the BackandLay email was strongly critical of the Betfair approach. It is obvious that the views of a more established business such as Betfair may not be the same as those of its emerging competitors.

146. The procedures adopted were not, in my view, conducive to good decision making. Furthermore, if the minutes accurately and fully record what was said, then, in two respects at least, the members of the Board were given information which was materially false (paragraphs 114 and 120).

Obligation to consult

147. Mr Pannick submitted that the Board was not required to consult the betting exchanges. In the words of his skeleton argument: "In the present context, Parliament has provided for a mechanism by which the views and interests of affected persons can be taken into account through the BC". That passage has to be read against the abandonment by Mr Pannick of the proposition that the Committee should inform the Board of all relevant matters concerning the interests of all bookmakers (paragraph 23 above).

148. Mr Pannick relied on the well-known passage from the speech of Lord Mustill in *R v Secretary of State for the Home Department ex parte Doody* [1994] 1 AC 531, 560D-G. What fairness requires depends on the context, and

> "An essential feature of the context is the statute which creates the discretion, as regards both its language and the shape of the legal and administrative system within which the decision is taken".

In my view, fairness required consultation with those liable to be adversely affected by the imposition of a tax by a statutory body such as the Levy Board. That consultation may, for certain groups, be effected through the Committee. However, neither the Board nor the Committee saw the Committee's task as being one which involved making representations to the Board on behalf of bookmakers not represented on the Committee. Furthermore the Board knew that the Committee did not represent the views of the betting exchanges. Indeed the Committee took the view that money which might otherwise have been channelled through the traditional bookmakers was being diverted through the betting exchanges, that the on-course market was being adversely influenced by some bookmakers laying off their liabilities through the exchanges, that the betting exchanges were reducing the amount of the levy and causing the theoretical £6m default (paragraph 26 above) and believed, in accordance with legal advice, that, in the context of betting exchanges, the activity of the layer was illegal and, therefore, the activities of the bettor and betting exchange operator were illegal too (paragraph 13 above). The Committee also supported the attempts by the BHB to set the licence fee on the same aggregated profitable layers basis. As Mr Ross had said on 12 September, the recommendations put forward by the Committee "were intended to be a mirror of the BHB commercial policy" (paragraph 28 above). Furthermore Mr Bartlett had expressed the view that the betting exchanges "were successfully operating as a result of a tax concession but once this was removed their businesses would founder" (paragraph 84 above).

149. It seems to me that the concerns expressed by members of the Board during this period about the lack of consultation and the threat of judicial review (see paragraphs 53, 55, 80, 84, 89, 103, 106, 108 and 111) reflect a fairer and more acceptable approach than that for which Mr Pannick now contends or for which Mr Bartlett, for example, contended particularly during the last meeting. Nor do I find attractive Mr Pannick's argument that it was for the claimant to seek an opportunity to be heard by the Board and not for the Board to consult the claimant. Whereas Mr Ross was given an opportunity, which he took, to make oral representations to the Board on behalf of the traditional bookmakers as represented on the Committee, the betting exchanges were not.

150. In my judgment the approach adopted by the Board and by Mr Pannick on its behalf to the issue of consultation is seriously flawed.

151. Although there was some consultation by Mr Brack, the Board's approach reflected the views now expressed by Mr Pannick- there was no obligation on the part of the Board to consult and, if consultation was to take place, that was a matter for the Committee and the Board had no power to direct the Committee. That approach is amply demonstrated during the meeting of October 31 when the Board invited the Committee on some four occasions to circulate the revised proposals to the betting exchanges and spread betting companies. The Committee refused the invitations at about 11.10 am (paragraph 104) and 2.00 pm (paragraph 126) for what, in my view, were not good reasons.

152. The fact that the Board was so concerned that the betting exchanges and the spread betting companies had not been sent the revised proposals demonstrates to me a deep unease about the effect of the proposals on the betting exchanges and the Board's unwillingness or perceived inability to deal properly with the proposals if that did not happen. This alone, in the context of this case, leads me to decide that the Board did not carry out the process of determining the levy in a fair or lawful manner and that my conclusion on this aspect of the case is sufficient to dispose of Mr Pannick's alternative argument that what happened in fact "was amply sufficient" to cure any procedural defects.

153. If I am wrong about this conclusion, I turn now to that alternative argument.

Did any consultation which did take place cure the procedural defects?

154. The obligation to consult being, in my view, on the Board, the Committee's consultation on 24 October can safely be ignored, particularly as the results of that consultation were not transmitted to the Board, except in so far as mentioned by Mr Bartlett during the meeting- a matter to which I return below.

155. As to the Board's obligations, the Court of Appeal in *R v North and East Devon Health Authority, Ex p Coughlan* [2000] 2 WLR 622, 661 provided helpful guidance:

> "To be proper, consultation must be undertaken at a time when proposals are still at a formative stage; it must include sufficient reasons for particular proposals to allow those consulted to give intelligent consideration and an intelligent response; adequate time must be given for this purpose; and the product of consultation must be conscientiously taken into account when the ultimate decision is taken…"

156. There was no consultation by the Board with the claimant other than at the meeting between Mr Brack and Mr Griffiths on 28 October, although Sporting Options were paying the levy and therefore registered with the defendant Board under the 41st scheme. As Mr Griffiths said in paragraph 38 of his witness statement (see paragraph 75 above):

> "I was very busy running Sporting Options at this time. In the short time available, I did not have the opportunity to prepare our case against the proposed Levy Scheme as thoroughly as I would have liked."

157. Mr Pannick criticises his failure to take steps and his "lack of vigour" and submits that "any lacuna" in the claimant's submissions was due to the fact that Mr Griffiths "left it" to Betfair. Mr Pannick also submits that even if the Board had sent the Committee's 30 October recommendations to Mr Griffiths, it is fanciful to suggest that he would have added anything, given that he says that he lacked the time to do any more. I do not agree. Having only recently launched Sporting Options live, it is fully understandable why he would be very busy, as he says he was. It is no answer to a failure to give adequate time, to say that he could have used the inadequate time more purposefully.

158. I add that Betfair, which was consulted earlier, also understandably complained about lack of time (see paragraph 57 above).

159. Neither Betfair nor Mr Griffiths were provided by the Board with the full 30 September recommendations, including the projection of £3.5 million, or with the edited portion sent to Betfair (which Mr Griffiths received on 31 January 2003). However, from his quick review on October 24 of the Betfair letter of October 15 (see paragraph 75 above), Mr Griffiths would have known what the Committee was recommending for betting exchanges and the reasons therefor.

160. On October 30, the Committee abandoned the "double levy", altered (at least superficially, see paragraph 93 above) the reasons for recommending a levy on successful layers but added in a further justification, namely that the proposals were fair and equitable. The Committee was now justifying the case for change on the basis that all layers on betting exchanges were "like bookmakers" and must therefore pay as bookmakers do, albeit that it is for the exchanges to collect the levy. The Committee for the first time dealt with double counting, with the consequences which I have described (paragraphs 31 and following). The Committee was no longer giving even the roughest guide as the estimated yield of the proposed levy on betting exchanges, the £3.5 million projection having been excised. None of this was known to Mr Griffiths, the Board having "noted" the Committee's refusal to accept the invitation to send the proposals to him.

161. Mr Griffiths was afforded no proper opportunity to calculate the financial impact of the proposals, as he was able to do during the judicial review application as part of the attack on the alleged irrationality of the scheme in so far as betting exchanges are concerned.

162. Mr Griffiths did not know that Mr Bartlett, Chairman of the Committee, took the view, expressed at the 23 October meeting of the Board (paragraph 84 above), that if the changes were made the business of the betting exchanges "would founder". Mr Griffiths' views were not transmitted by Mr Brack to all members of the Board and, if the minutes accurately reflect what Mr Bartlett said, were seriously misrepresented.

163. Mr Griffiths puts it this way in his first statement:

> "42. Reviewing the comments I made at the meeting of the Bookmakers' Committee and a paper I asked to be read by the Levy Board, I considered that I did my best at short notice (I had just three full days before the meeting of the Bookmakers' Committee) on a complicated area to make the position of Sporting Options known. However, I consider that if I had been consulted properly on the proposals and if I had had more time to prepare I believe that I could have made the points I did make more forcefully and further points as follows:
>
> I would have been able to calculate the economic impact these proposals would have on the business of Sporting Options by reference to our past performance.
>
> If I had been provided with the reasons for the proposed change in the Levy, I would have been able to consider and address them and suggest alternative options which may have achieved the same ends without causing such harm to the business of Sporting Options.
>
> I would have pointed out that the Levy Scheme proposed discriminated against betting exchanges compared to traditional bookmakers.
>
> I would have pointed to the particularly severe impact of the proposed Levy Scheme on new entrants in the market.
>
> 43. Moreover, I do not consider that the approach made to and consultation afforded to Betfair by the Levy Board was in any way an adequate substitution for consultation with Sporting Options. Betfair is a different company and while we are both betting exchanges, it is in a radically different position in the market and the impact of the proposed changes on its business and on our own is very different. Indeed, I believe that the fact that Betfair was given a much better opportunity to put its views forward to the Bookmakers' Committee and the

> Levy Board than we were skewed the consultation against us. For example, the Bookmakers' Committee and the Levy Board may have given considerable weight to Betfair's preparedness to accept in principle a Levy assessed on aggregated profitable layers (but subject to a cap) although we strongly opposed this. I can see no justifiable reason why we were not consulted on the proposals equally with Betfair."

164. To many of the points raised by Mr Griffiths, I return shortly. They have considerable merit. Miss Rose submits, and I agree, that there is a striking difference between the procedure followed by the defendant and that that would have been followed by the Secretary of State as described by Mr Brack in his first statement at paragraph 15:

> "In the event (as occurred last year) that the new scheme has to be referred to the Secretary of State for determination, the following steps take place, before the administrative steps for implementing the new scheme can occur (under a compressed time-frame to meet the 1 April start-date). Again, this is well-known within the industry.
>
> 1) The Secretary of State writes to all interested parties, such as the BHB and the Committee, inviting them to make representation on the terms of the new scheme. Representations are generally made in writing, although if expressly requested, and the Secretary of State deems this to be appropriate, oral representations may be made in addition to or instead of written representations. The process of requesting and receiving representations generally takes three to four weeks.
>
> 2) The Secretary of State may then appoint external economic consultants or chartered accountants in order to assess various aspects of the submissions received from interested parties, and/or related issues, and advise.
>
> 3) The Secretary of State's officials at the Department of Culture, Media and Sport will then consider the representations and any expert reports before putting recommendations before her for the determination of the new scheme. Altogether, this process can take several months."

165. In my judgment the suggested guidance given in *Coughlan* was not followed and the procedural defects were not cured by what did take place.

166. It is further submitted on behalf of the defendant that, notwithstanding any procedural defects, there was no material unfairness in that the Board did fully consider the issues raised by the Betfair letter, was aware of the Sporting Options position and this was sufficient. In my view this submission could not succeed given the procedural defects. I shall, however, consider it.

The defendant's submission that, notwithstanding any procedural defects, there was no material unfairness

167. It is submitted that the members of the Board fully considered the issues raised by Betfair and understood that the claimant opposed any change. As Miss Rose pointed out, the claimant, a new entrant into the market, was not in the same position as its more established competitor and was entitled to be heard in its own right.

168. Miss Rose in her reply put her case in this way:

> "[The claimant] submits that … the decision of the Board on 31 October 2002 to adopt the scheme was irrational, since it was taken by the board without the benefit of essential information, or a proper understanding of centrally relevant matters, and without any consideration of the issues that arose, or any conclusions being reached in relation to them. The Board failed to ask itself the right question, or to take reasonable steps to obtain the information necessary to answer that question."

169. If the Board fully considered the issues, that is not reflected in the minutes and indeed, as Miss Rose submits, the Board could not have fully considered the issues given the absence of important information.

170. There was no discussion recorded in the minutes as to the various justifications which the Committee had given during the two month period to justify the change. One of the justification for the recommended levy on betting exchanges was that the margins of bookmakers were being reduced by the betting exchanges as well as the alleged shortfall in the levy being caused by betting exchanges (see paragraph 95 above). The minutes do not record any discussion about that and there was a complete absence of material to support that contention.

171. Even if that were right, why should the levy be related to successful layers? The answer given by the Committee on October 30, was that layers on betting exchanges are like bookmakers. There was no recorded discussion of this issue (or indeed of the change in the position of the Committee since September), except in so far as it was raised by Mr Jones when he said that he believed that the Committee was attempting to align the payment by betting exchanges with the payment by bookmakers, to which the Chairman gave the enigmatic answer: "that it was important not to double guess the Committee's motivation" (see paragraph 117 above). There was no recorded discussion of section 27(2)(a) which provides that the levy shall be payable only by a bookmaker who carries on, on his own account, a business which includes the effecting of betting transactions on horse races. Without giving a definitive answer to the question of the lawfulness of the proposed scheme in so far as successful layers are concerned, there must, at the least, be doubts. Given that layers, other than those in the business of effecting betting transactions, are not bookmakers then the rationale given by the Committee (and by Mr Bartlett in his first witness statement) for the assessment of the levy on the gross profits of layers on betting exchanges would appear to be considerably weakened.

172. There was no recorded discussion as to how the betting exchanges were expected to impose the new levy on successful layers. Two routes were possible: impose the levy on the successful layers or make any necessary increase to the commission paid by backers and layers. The former would obviously make laying unattractive, and even more so if unsuccessful backs could not be set off, and would thus jeopardise if not undermine the viability of the betting exchanges, (see paragraph 67 above) particularly for new entrants. This may be what Mr Bartlett was referring to when he spoke of the betting exchanges foundering (see paragraph 84 above).

173. During the course of the case, the worked examples proceeded on the assumption that the exchanges would be likely to increase the commission payable by both layers and backers. If that is the only sensible way of meeting the new levy, then that, as Miss Rose submitted, undermines the justification for the change.

174. If the commission on layers and backers would have to be increased to meet the new levy, there was no recorded discussion of the difficulties which the betting exchanges would face in calculating the commission to charge, given Betfair's contentions that the new levy would, both in the short term and over the year, "generate an extremely volatile liability which it would be impossible to predict" as well as lay the exchanges open to sabotage by disgruntled punters or competitors (see paragraph 67 above). There was no recorded discussion of volatility,

vulnerability or the need for a cap. If the minutes are accurate, then the Board was being misled about both the position of Betfair and of the claimant (see paragraph 114 above).

175. Both the Board and the Committee, in argument, cast doubt on the volatility/vulnerability to sabotage argument. It was submitted that procedures could be put into place to avoid sabotage. That submission may be right or wrong (and I suspect that it is wrong), but certainly requires consideration. It was further submitted that, if there were problems, then the matter could be reviewed when the 43rd scheme was being considered. This is hardly a satisfactory answer to an allegation of lack of consultation. The claimant's submissions are clearly strongly arguable, as shown by the following passage in a May 2003 Government paper (3/362, at 363), in which the Government announced its intention to require betting exchanges to pay duty of 15% of their commissions:

> "3.10 In proposing alternative GPT arrangements for exchanges many respondents (primarily representing traditional bookmakers) argued that the principle of treating all exchange layers as bookmakers for duty purposes should continue. The one change they advocated was to move away from the process of aggregating the position of all layers over the month, to taxing the profits of just winning layers.
>
> 3.11 The Government has decided not to adopt this approach. This is because it would fail to address the fundamental flaws with current arrangements, for example the lack of any direct link to an exchange's revenue and the volatility of duty liability, indeed these problems would be exacerbated. Had duty been based on the aggregated profits of winning layers the effective rate of tax [15% of the profits of winning layers] for exchanges during 2001-02 would have exceeded 30% [of the commission], threatening the business model.
>
> 3.12 The main alternative is to levy duty on an exchange's commission – effectively the real gross profit for operators. This would relate tax to ability to pay; it would address concerns about the volatility of duty payments under the current system; and liabilities could not exceed commission.
>
> 3.13 The Nottingham Universities conclude that such an approach would be fairer and more efficient than the current system. All betting exchanges that responded to the evaluation believe this approach would be appropriate."

176. Miss Rose submits:

> "Further, the Decision discriminates without justification against betting exchanges. Betting exchanges are being less favourably treated than traditional bookmakers, who are to be charged the Levy on the basis of 10% of their own gross profits. Traditional bookmakers [unlike the exchanges] are thus to be taxed on a basis that is by definition proportionate to their profits, at a reasonable level, predictable, and not vulnerable to abuse. (Paragraph 80 of claimant's skeleton argument)"

Whether Miss Rose is right or wrong, the issue certainly requires detailed consideration.

177. The Board had no information upon which it could determine how much levy would be raised from Sporting Options, Mr Griffiths having been afforded no proper opportunity to calculate the financial impact of the proposals. Time was spent during the hearing analysing figures produced by Mr Griffiths. It is sufficient to say that, in the period covered by the figures, the claimant would have had to increase its commission on all punters by 34% to meet the levy. Applying the 42nd

levy scheme to the figures in the May 2003 document (see paragraph 175 above), the amount of the levy as a percentage of the average commission charged by betting exchanges (the figures for which were available) would, as I understand the mathematics, have doubled from 10% to 22%. In the words of Miss Rose commenting on the 34% figure (Reply, paragraph 26):

> "The impact on any new business, competing with a very well established rival (Betfair) of being forced to raise its prices by one third is self-evident. If the Claimant could compete with prices one third higher than they are currently set, it would already be doing so. The difficulties are particularly great in this market, since an exchange cannot operate without a large enough pool of customers to generate a market. The business is extremely price sensitive, particularly for new, smaller exchanges, yet the 42nd scheme has the greatest impact upon them (see Griffiths at 1/81, paragraph 52(b)). In short, the increase in commission is very significant, and is likely to hit disproportionately at new entrants. The 42nd scheme is a very significant barrier to entry."

178. In Miss Rose's words:

> "The members did not even have the benefit of an "educated guess", as to the amount that would be raised, as was acknowledged on 31 October 2002 [paragraph 109 above]. This is in contrast to the efforts made by the Defendant to verify the BC's estimates of the share of horserace gross profits in total betting gross profits, which were subjected to independent analysis … . It also contrasts with the treatment of Spread Betting Companies. The Defendant decided to leave the basis for the assessment of the Levy on Spread Betting Companies unchanged, on the ground that more research was required into their operation: [see October 31 letter from Committee, paragraph 136 above]."

179. In the case of the spread betting companies, the Board were able to assess the amount of the proposed increase as the 31 October minutes show (paragraph 108, above):

> "[The Chairman] said that the proposed levy rate of 10% represented a 400% increase over the Secretary of State's determination in March of 2%."

180. Mr Pannick pointed to the Betfair figure (paragraph 67 above) that the original dual basis would have generated liability for levy in the period April to September 2002 equal to approximately 19% of Betfair's commission over the same period. Extracting the 10% following the abandonment of the dual levy, would leave 9%. It seems unlikely, having regard to the discussions (paragraph 109 above) that the Board relied on this figure, which, if right, would have led to a reduction in the levy (Betfair having 90% of the business and charging higher commission rates than Sporting Options). Given that the Committee was trying to redress the alleged shortfall of £3 to £4 million in the levy caused by the betting exchanges (see paragraph 25 above), it seems very unlikely that the Committee thought that the levy from the exchanges would be less than under the 41st scheme. In any event Betfair made it clear given the potential volatility of the profitable layers' basis and liability to sabotage, Betfair was unable to predict its effects. As Betfair wrote (pargagraph 65 above):

> "The new element in the BC Submission (i.e. 10% of all profitable layers' profits) would however generate an extremely volatile liability which would be impossible to predict. In many circumstances, levy liability will greatly exceed commission revenue generated by the betting exchange; indeed in any races where an odds on favourite loses, the levy liability generated will be many times greater than the commission revenue generated."

181. Mr Vajda also sought to rely on the figures for the estimated yield under the 41st scheme in the September 5 letter (said by Mr Brack to be treated with some caution, see paragraph 48 above) and the suggested yield of up to £3.5 million referred to in the September recommendations. Not only did that figure include two other groups but the figure was not only not re-worked for the October 30 recommendations, it was abandoned (having been included in the draft, although the Board would not have known that) (see paragraph 95 above).

182. There was no discussion recorded in the minutes of the impact that the proposed levy would have on the viability of betting exchanges or on competition, as graphically set out in the BackandLay letter which was not given to the members of the Board or as set out in the witness statement of Mr Williams of Betfair in these proceedings:

> "Just because betting exchanges tend to make smaller margins by charging 'minimal commission' does not mean that it is fair to impose a different basis of tax just as it would not be fair to impose on Ryanair a different basis of corporation tax than British Airways."

183. That was particularly important given that the traditional bookmakers, as the justification for the September recommendations show, disliked the betting exchanges and saw them as a threat to traditional bookmaking and took the view that layers on betting exchanges fell within the statutory definition of "bookmakers" and thus needed a permit (see paragraph 13 above).

184. There was no recorded discussion about the removal of the "double counting" error and thus no discussion about permit holding bookmakers passing on their liability under the 41st scheme to betting exchanges or sharing their liability under the 41st scheme with fellow backers and layers. In Miss Rose's words:

> "Further, traditional bookmakers are permitted to lay bets through exchanges without paying the Levy on their profits, and thereby to pass on their liability for Levy to betting exchanges." (Paragraph 80)

185. In the words of Mr Griffiths (second statement, paragraphs 10 and 11):

> "… under the 42nd scheme, licensed bookmakers are not liable to be assessed for the levy on any profits they make through laying bets on betting exchanges. Instead, the exchange (which may have earned no commission from their bets) is liable to pay the levy on the bets laid by the profitable licensed bookmaker.
>
> The amount of the levy due is assessed purely on the basis of the bookmaker's performance on the exchange. The result is that if a bookmaker has made a loss laying bets through his betting shop, but has made an equal profit laying bets on an exchange, the bookmaker has no liability to pay levy, while the betting exchange is liable to pay the levy on the bookmakers' profits on the exchange, without being able to set off the losses made through his betting shop. "

186. Neither Betfair nor Mr Griffiths knew about the removal of the double counting "error", which only surfaced on 30 October.

187. There was no discussion recorded in the minutes of the differences between the "aggregated profitable layers basis" and the "aggregated layers basis" nor of the possible consequences of adopting the former on the viability of betting exchanges and the risk to them of sabotage by those with a grudge or those anxious to help a competitor. If the minutes accurately record what Mr Bartlett said about the position of Customs and Excise (paragraph 120), other members of the Board would, on the face of it, have been misled. According to Betfair over extended periods "the

aggregated position of layers will tend to zero" (paragraph 70 above and see also the BackandLay email, at paragraph 89 above). According to the later May 2003 paper, moving from an "aggregated layers basis" to an "aggregated profitable layers basis" led to a six fold increase in the amount payable.

188. The minutes record no discussion of the following point made by Miss Rose (Reply, paragraphs 18 and 20) about the new scheme:

> "18. … If a customer uses more than one exchange as a layer, he cannot offset losses he makes on one exchange against profits he makes on another. By contrast, a bookmaker with a chain of shops may offset losses made in one shop against profits made in another. Thus, an individual who lays bets on exchanges may incur a substantial levy liability even though he has made no profit from laying bets on horseracing. This cannot happen to a traditional bookmaker under the 42nd Scheme, who is only taxed on the overall gross profit he has made from laying bets on horseracing.
>
> 20. This particular element of the 42nd Scheme will seriously impede the efforts of new betting exchanges to enter the market, if the levy is to be passed on to layers. Customers wishing to lay bets (as the great majority do) are much less likely to experiment or use more than one exchange, if in doing so on an infrequent basis they risk building up a large levy liability which cannot be offset against their losses on other exchanges. "

189. Thus, so Miss Rose submits, the scheme treats layers less favourably than bookmakers. Whether she is right or wrong, the point she makes needs consideration and probably depends on a study of the recommendations as a whole, something which was denied to the betting exchanges.

190. Mr Pannick submits that it would be wrong to place much reliance on the contents of the minutes, otherwise the minutes would become a necessary substitute for reasons. He points out that the Claimant was not submitting that a reasoned decision should have been given. I do not agree that it would be wrong to place much reliance on the minutes. Given what I have found to be a flawed procedural approach to the process of setting the levy, it must be for the Board to show that what happened in fact "was amply sufficient" to cure any procedural defects. In that context, the minutes are of considerable importance.

191. Both the Board and the Committee rely on the witness statements of those involved as showing that the minutes do not accurately reflect what happened. I turn to them now.

192. Mr Hughes, the Chairman, wrote in his statement dated 4 June 2003, prepared during the hearing:

> "2. I understand that a point has arisen as to whether a minuted comment of Mr Bartlett misled members of the Board as to the position of betting exchanges, and in particular into thinking that Betfair had dropped its insistence on a cap and that Sporting Options had dropped its insistence on a commission-based levy.
>
> 3. Betfair's insistence on a cap was set out in its written submissions with which Board Members had previously been circulated. Sporting Options' insistence on a commission-based levy had been communicated to me and to the two independent members at a briefing with Mr Brack who had met with a representative of Sporting Options [confirmed by Mr Brack].

> 4. I did not take it, from any comment made at the meeting or otherwise during the day, that this position had changed.
>
> 5. Moreover, I can say from my recollection of the formal discussions and the informal discussions which took place in between the formal sessions of the meeting, that I was and I believe all the Board members were aware in general terms of the position of Betfair, Sporting Options and Betdaq [another betting exchange] in relation to contributions by them to the levy."

193. Mr Bartlett wrote in his second statement:

> "3. The minutes of the Levy Board meeting on 31 October … were not a verbatim account. The meeting commenced at 11am and as I recall, did not finish until approximately 6.45pm. Though of course there were a number of adjournments during which individual members discussed various issues, the notes only consist of some 8 and a half pages of text and represent only a summary of the discussions which took place between Levy Board members at the meeting. Moreover, the notes do not include reference to discussions between Levy Board members which took place during the various adjournments."

194. He then addressed the alleged misrepresentation about the views of the betting exchanges:

> "4. The record indicates that I confirmed, in response to a question concerning the capacity of betting exchanges to pay levy, "that the betting exchanges were willing to pay either on an assessment of the profits of their successful layers, or on their gross commissions, but not on both." No doubt, in isolation, this statement can be interpreted in many ways, and to many ends, as the Claimant has sought to do. However, in addition to the fact that this is only a summary minute, the statement must be considered within its proper context.
>
> 4.1 There is no way that anyone present at that meeting of the Levy Board on 31 October could have been under the impression that betting exchanges, whether as a group or individually, agreed with the recommendations of the Bookmakers' Committee. I have seen and agree with what is said in Herbert Smith's letter of 29 May 2003 on behalf of the Levy Board. Notably, Levy Board members were fully aware of Betfair's views (including the apparent need for a cap) after its letter of 15 October had been circulated to them. Also, Rodney Brack of the Levy Board received a discussion note from Mr Griffiths on 30 October which clearly indicated that in his view betting exchanges should not be asked to pay more than 10% of their revenues (i.e. commission) in levy (see RLB2 page 205). The Levy Board was well aware that neither the views of Betfair nor the Claimant had changed since their written communications.
>
> 4.2 Moreover, there was considerable discussion of the views of the exchanges on the day. As is the case each year, this meeting of the Levy Board was characterised by discussions on certain subjects and then adjournments, during which all the parties took time to consider and discuss with each other, generally in smaller groups, matters of disagreement between them. During such adjournments, there was discussion of a number of contentious matters including the position of betting exchanges, the desire of Betfair to cap its levy liability and the desire of the Claimant to pay on the basis of the 41st Scheme. I certainly personally discussed the views of the exchanges with the Chairman of the Levy Board (who reports back to the other independent members), with Mr

> Peter Jones (Chairman of the Tote) and with those representing the British Horseracing Board. This is usual practice. No member of the Levy Board can have been in any doubt whatsoever that betting exchanges were not happy with the recommendations of the Bookmakers' Committee insofar as they affected them. Moreover, there is no question that the issue of Betfair's preference for a cap on its liability was discussed.
>
> 5. In summary, my statement was a fair reflection of the position against a background of considerable discussion and debate about and knowledge of the position of the betting exchanges. I cannot recall a levy where all parties subject to it have been happy with the recommendations of the Bookmakers' Committee. The 42nd Levy Scheme was no different.
>
> 6. By indicating that exchanges were prepared to pay on one particular basis or another, I certainly did not intend to give the impression, nor do I believe I gave such an impression, that the Claimant specifically was prepared to pay on the basis of its layers' profits."

195. Mr Bartlett addressed the other alleged misrepresentation:

> "8. It is alleged that I wrongly stated that the basis proposed in the Recommendation of the Bookmakers' Committee was different only in detail from the basis on which betting exchanges are assessed for gross profits tax by Customs and Excise … The important point I was making was that the Recommendation was based on assessing *profits from layers rather than on commission* and in that respect was similar to the method of assessment of GPT used by Customs & Excise."

196. In his second witness statement dated 16 May 2003 Mr Brack went through the minutes of the 31 October in great detail but did not make comments similar to those made by Mr Bartlett in the passages from his later statement which I have set out. I have already referred to his post-hearing comments on the BackandLay email (paragraph 89 above).

197. Courts treat with caution witness statements explaining a decision for the obvious reason that there is a risk that, albeit unconsciously, a decision maker may seek to remedy any apparent weakness. I turn to the first alleged misrepresentation. I accept that the members of the Board were aware "in general terms", to use the words of Mr Hughes, of the position of the betting exchanges. If the members had thought that the betting exchanges were as content with the proposals as this comment suggests, then there would have been no need for any discussions. I accept that Mr Bartlett discussed the views of the exchanges with the Chairman, and thus the independent members, Mr Jones and the BHB members. Mr Pannick submits that the Board had the Betfair letter and was therefore fully acquainted with the issues. Miss Rose submits that the members were not to know whether what Mr Bartlett was saying reflected at the least a softening of Betfair's position following the October 24 meeting, of which the Board had no minutes. Indeed the summary of the views of the exchanges at the meeting had been excised from the Committee's October 30 letter (see paragraph 23 above). The fact that this minute went uncorrected by any member of the Board seems to me to be important. If there had been the kind of in-depth analysis of the issues which, in my view there ought to have been, it is difficult to believe that no member of the Board would have left this minute uncorrected. The minutes do not reflect any discussion of the outright and unchanged opposition of Betfair without a cap as expressed in the October 5 letter and the outright opposition of Mr Griffiths and, more importantly, the substantial justifications for their position

198. As to the alleged misrepresentation (paragraph 120 above) the evidence given by Mr Bartlett and by Mr Brack does not convince me that the members of the Board properly considered these difficult issues. Again I note that the minute went uncorrected.

199. For all these reasons I conclude that the manner in which the Board reached its decision on 31 October was manifestly unfair.

Other grounds

200. Miss Rose submits that the Committee were motivated in their proposals by an improper desire to alter the competitive balance between the traditional bookmakers and the betting exchanges and that the Board adopted the recommendation to achieve this. Mr Bartlett, as Mr Vajda stresses, has made it clear in his witness statement that he believed that the proposals were fair and equitable and Miss Rose did not seek to cross-examine him about this. It seems to me clear that Mr Bartlett and the Committee blamed the betting exchanges for taking away business from the bookmakers and thus reducing the levy, but they did so because they thought, wrongly or rightly, that the playing field was not level. They sought to make it level by their proposals. I reject this ground. Nonetheless the Committee must bear some responsibility for what, in my view, went wrong in the setting of the 42nd levy.

201. Miss Rose submits that the decision of the Board was substantively irrational and that there was a breach of both domestic law and the EC Treaty. The argument on substantive irrationality which is tied up with the other grounds, is obviously a strong one, but, given my conclusions, I do not need to resolve these issues and could not on the material available to the Board.

Conclusion

202. But for the fact that only declaratory relief is now sought (see paragraph 4 above), I would have quashed the decision for the reasons which I have given. I shall now hear argument on the issue of what order I should make.