

Kentucky Horse Racing Authority Calendar Year 2006 Annual Report

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Commissioner

Lisa E. Underwood
Executive Director

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MISSION OF THE KENTUCKY HORSE RACING AUTHORITY

On January 6, 2004, the Kentucky Horse Racing Authority (KHRA) was created and established as an independent agency of state government charged with the responsibility of regulating the conduct of horse racing and pari-mutuel wagering on horse racing and related activities within the Commonwealth of Kentucky.

The Authority consists of 13 members appointed by the Governor, with the secretaries of the Environmental and Public Protection Cabinet, Commerce Cabinet and Economic Development Cabinet serving as ex-officio nonvoting members. One member is appointed to serve as chairperson of the Authority. A second member is designated to serve as vice chair of the Authority to act in the absence of the chair.

Pursuant to Governor Fletcher's Executive Order establishing the Authority, the KHRA is responsible for the following:

- a) Developing programs and procedures for oversight and regulation of horse racing matters, including, but not limited to, race day medications.
- b) Recommending tax incentives and other options to promote the strength and growth of the thoroughbred industry and to preserve the economic viability of Kentucky's horse farms.
- c) Designing and implementing programs that strengthen the ties between Kentucky's horse industry and the state's universities, with the goal of increasing the economic impact of the horse industry on Kentucky's economy.
- d) Developing and supporting programs that ensure Kentucky remains a national leader of equine research.
- e) Developing and implementing programs that promote Kentucky's horse and tourism industry.

Kentucky Horse Racing Authority at a Glance

The **Kentucky Horse Racing Authority (KHRA)** is the state agency in Kentucky responsible for regulating and promoting our Commonwealth's signature industry. KHRA is privileged to administer programs designed to benefit all Kentuckians involved in horse racing, whether they be horse owner, trainer or the occasional two dollar bettor.

KHRA is an independent agency attached to the Environmental and Public Protection Cabinet for administrative purposes, and is comprised of an Executive Director and staff, and a 16 member Board.

Executive Director, Lisa E. Underwood assumed leadership of KHRA on October 2, 2006, and has continued to implement changes to enhance KHRA's ability to fulfill its regulatory mission. Director Underwood supervises a 21 member full-time staff of racing professionals including the chief steward and chief judge, veterinarians, detention and security personnel, and administrative and licensing staff. KHRA is governed by a 16-member Board which is comprised of 13 voting and 3 nonvoting members from Governor Fletcher's Cabinet. KHRA is honored to have the following racing industry and community leaders serve as voting members of the Board:

Chair William Street, Chair and former President and CEO of Brown-Forman Beverages, continues as a member of the Brown-Forman Corporation Board of Directors, where he has served since 1971. Mr. Street is a graduate of Princeton University and the Harvard Business School.

Vice-Chair Constance Whitfield of Hopkinsville was a former attorney for the U. S. Department of Justice and Office of Legal Policy. A Phi Beta Kappa and cum laude graduate of Stanford University, she holds Bachelors and Masters Degrees from Stanford and a Juris Doctorate Degree from the University of California at Los Angeles. Mrs. Whitfield is the Chair of the Equine Drug Research Council.

Mr. Kerry Cauthen received his undergraduate and law degree from the University of Kentucky. Kerry is a co-owner and managing partner of Four Star Sales with John T.L. Jones, Jr., Dan Kenny and David Greathouse. Kerry serves on the board of the Consignors & Breeders Association (CBA), a trade organization that represents thoroughbred consignors and breeders in educating the market participants in matters relating to horse sale rules and regulations. He is a member of the Keeneland Association and Thoroughbred Owners and Breeders Association (TOBA). He is a former Chairman of the National Thoroughbred Racing Association (NTRA) Communications Committee, a member and former director of the Kentucky Equine Education Project (KEEP), the Thoroughbred Club of America and a Director for High Hope Steeplechase.

Mr. Thomas Gaines is a veteran executive in the thoroughbred industry. Mr. Gaines currently serves as president of KBC International, a worldwide horse equipment

company. He is a founding partner in Gaines-Gentry Thoroughbreds and also partnered in Paramount Sales Agency. Additionally he serves on the Board of The Breeders Cup as well as the (NTRA). Mr. Gaines is also active in KEEP.

Ms. Dell Hancock is a co-owner of Claiborne Farm in Paris, Kentucky. She is currently a member of the Board of Directors for the Kentucky Thoroughbred Association (KTA), a member and steward of the Jockey Club, Chairman of the Grayson Foundation and Chairman of the American Graded Stakes Committee. Ms. Hancock is also a member of the Commission of the Kentucky Horse Park.

Mr. Doug Hendrickson currently owns numerous thoroughbreds in various partnerships. He received a Bachelor of Science from the University of Georgia and graduated from Rutgers University/ABA with a graduate degree in Banking and Finance.

Mr. Tom Ludt is co-general manager of Vinery, Ltd., a stallion farm located in Lexington, Ky., and Ocala, FL. He serves on the Board of Trustees for the Breeder's Cup and is a newly elected board member of TOBA. Mr. Ludt is a member of the Sales Integrity Task Force.

Mr. Larry Telle has been with the investment firm of J.J.B. Hilliard, W.L. Lyons Inc. for more than 27 years. His role as Senior Vice-President includes investing for individual and corporate clients as well as principal trading NASDAQ stocks in the over-the-counter market. Mr. Telle holds a Bachelor of Science degree in Economics and Political Science from the University of Kentucky. He has been an owner and breeder of thoroughbred race horses since 1984, including stakes winners *Double Zero Seven* and *Longsuit*. Mr. Telle currently serves on the Board of Directors of the Association of Racing Commissioners International Inc. as well as other civic boards.

Mr. Kenneth Alan Jackson of Lexington was appointed in December 2006 and is an attorney and owner of Kentuckiana Farms. Mr. Jackson is a graduate of the University of Kentucky and received his Juris Doctorate from the University of Louisville. He is a member of the Board of Directors of KEEP, the United States Trotting Association, the Thoroughbred Club of America, TOBA and the Kentucky and Fayette County Bar Associations.

Dr. Jerry Yon was appointed in December 2006 and is a self-employed physician. Dr. Yon is a graduate of the University of Illinois, the University of Kentucky College of Medicine and the University of Illinois Medical Center. He is a member of the Lexington Medical Society, the Kentucky Medical Association, the American Society of Gastrointestinal Endoscopy, the American College of Gastroenterology and the Thoroughbred Club of America.

Mr. Franklin Kling was appointed in December 2006 and is Chairman and CEO of FK Holdings Inc. He received a Bachelor of Arts degree in Accounting from Thomas Moore College in Crestview Hills, Kentucky. Mr. Kling is an owner and breeder of

thoroughbreds in the Lexington, Kentucky area and is a member of Kentucky Thoroughbred Owners and Breeders (KTOB), the Kentucky Thoroughbred Association (KTA), the Kentucky Thoroughbred Owners & Breeders Association, the Thoroughbred Club of America and the Keeneland Club.

Mrs. Donna Smith is a graduate of High Point College and a former social worker and psychological assistant.

Mr. John Cashman served as former president and general manager of Castleton Farm. His term with the KHRA expired November 2006.

Mr. Tom Handy is retired Commonwealth's Attorney for the 27th District whose term with the KHRA expired in November 2006.

Mr. Jack Steinman is president of Rhinelander Inc. His term with the KHRA expired November 2006

Mr. Ben Walden is founder of Vinery Ltd. His term with the Kentucky Horse Racing Authority expired November 2006.

Ex-Officio Members (nonvoting)

Ms. Teresa J. Hill is Secretary of the Environmental and Public Protection Cabinet; her efforts are focused on helping Governor Ernie Fletcher grow Kentucky's economy and protect Kentucky's environment. She previously served as Vice Chairman of the Kentucky Public Service Commission. She also has served Governor Fletcher as executive director of boards and commissions and executive director of legal services in the Commerce Cabinet. Ms. Hill is an attorney and a former journalist and practiced law in Corbin, Ky. prior to entering public service.

Mr. Marvin E. "Gene" Strong Jr. began his tenure with the Cabinet for Economic Development as Deputy Secretary in December 1991, under former Governor Brereton Jones and was named Secretary of the Cabinet in March 1993 by the Kentucky Economic Development Partnership Board. Prior to joining the Cabinet, Strong spent 11 years as executive vice president for a national real estate development company based in Lexington, Kentucky, where his duties included marketing and negotiating office and industrial real estate transactions throughout the U.S. He successfully negotiated and finalized real estate transactions with many of America's Fortune 500 companies.

Mr. George Ward was appointed Secretary of the Kentucky Commerce Cabinet replacing Jim Host. He was formerly Commissioner of Kentucky Department of Parks. Mr. Ward spent 25 years in the hotel management business and began working in various hotel jobs at the age of 16. Mr. Ward graduated from Cornell University's School of Hotel Administration.

LETTER FROM CHAIRMAN STREET

I am privileged to submit this 2006 annual report of the Kentucky Horse Racing Authority (KHRA). I have been honored to serve as Chairman of the KHRA this past year assisting with the many challenges the Authority has faced and also the wonderful accomplishments we have achieved.

On January 1, 2006, Kentucky thoroughbred breeders began earning incentives through the newly established Kentucky Breeders Incentive Fund (KBIF) initiated by Governor Ernie Fletcher. KBIF awards monies to breeders who breed their mares to Kentucky stallions and keep them in Kentucky until they are foaled. The Breeders' Incentive funds will reward participants in the thoroughbred, standardbred and non-race breeds industries. Awards have been made in excess of \$15 million in total to these programs.

Working diligently with the racing associations, in 2006 the Authority was able to negotiate a settlement of the accounts relating to the Kentucky Thoroughbred Development Fund (KTDF) after a shortfall had been discovered that originated in the late 1990's.

In 2006, for the first time in many years, the KHRA reviewed and enacted various regulations for the thoroughbred and standardbred industry to protect the racing community and betting public. The new and updated regulations bring Kentucky to the forefront of regulatory rule and set forth precedents for other racing jurisdictions and future generations of regulators. Work on updating regulations is ongoing.

Part of the KHRA's mission is to develop programs and procedures in the regulation of race day medications. We are all concerned about the safety and health of every equine and human athlete that steps foot onto Kentucky race tracks. The KHRA approved the adoption of withdrawal guidelines for therapeutic equine medications to assist Kentucky's horsemen and veterinarians in the proper procedures in medicating their horses.

Over the past year the KHRA has made a significant effort to reorganize itself to improve the quality of service to our customers and licensees and to better serve the racing industry. The KHRA needs more personnel to help our signature industry grow and move forward in making our product the best racing has to offer. The need for an Equine Medical Director, a Supervisor of Pari-mutuel Wagering and additional enforcement personnel are essential to protect the integrity and fairness of horse racing in Kentucky.

These are just a few of the KHRA accomplishments during 2006 but there are many more challenges to be met.

Securing funding for the KHRA is a top priority which must be addressed if the Authority is to fulfill its mission of providing oversight to horse racing and developing programs that promote Kentucky's horse and tourism industry. Technology waits for no one and we must use every technological advancement to create a new fan base and educate our younger generations to the wonderful world of horse racing!

The Kentucky Horse Racing Authority desires to continue working in every way with all segments of the industry, the General Assembly and with Governor Fletcher to secure jobs for Kentucky in the racing industry and to protect the integrity of horse racing and keep Kentucky's claim as "The Horse Capital of the World!"

Sincerely,

A handwritten signature in black ink, appearing to read "William Street". The signature is written in a cursive, somewhat stylized font. The first name "William" is written in a large, flowing script, and the last name "Street" is written in a slightly smaller, more upright script. There is a vertical line separating the first and last names.

William Street

Executive Director's Comments

I am happy to report that the KHRA made great strides during 2006 and we are dedicated to continuing this record of achievement.

Since "taking over the reins" of KHRA on October 2, 2006, I have been privileged to work with a professional staff and an outstanding Board dedicated to regulating and promoting the Commonwealth's horse racing industry. The following are a few highlights from 2006:

- Throughout 2006, the KHRA continued to update the regulatory framework for the horse racing industry in Kentucky.
 - The Equine Drug Research Council recommended and the KHRA approved the adoption of withdrawal guidelines for equine medications which were incorporated into the revised penalty regulation.
 - An emergency regulation was filed relating to the Kentucky Thoroughbred Breeders' Incentive Fund (KBIF) so that breeders would qualify for awards beginning on January 1, 2006. During the inaugural year of the Thoroughbred Breeders' Incentive Fund, 1,789 Kentucky breeders qualified for a total of approximately \$12.6 million in award money. Jamie Haydon came on board during the summer of 2006 and did a tremendous job of making the new fund operational. See "Kentucky Breeders' Incentive Funds."
 - The jockey advertising regulation was amended to clarify permitted advertising. All of the jockeys were able to comply with the regulation during the Derby and the Breeders' Cup.
 - Thirty-three regulations were filed covering the standardbred industry. In addition, one regulation relating to the non-race breed incentive fund and one regulation authorizing the establishment and licensing of HUBs was filed. Also an amendment to the jockey advertising regulation was promulgated. All of the above regulations, as well as the regulation relating to KBIF have gone into effect.

- In March, the KHRA requested that the Office of the Auditor of Public Accounts audit the Kentucky Thoroughbred Development Fund (KTDF). The KHRA had become aware that there was a shortfall in the KTDF which began in the mid 1990's. Money from the KTDF supplements purses to the owners of horses bred in Kentucky and registered with the Kentucky Owners' and Breeders' Association Inc. These purse supplements are an integral part of the racing structure in the

Commonwealth. In December, the KHRA approved a settlement agreement and Memorandum of Understanding among the four major thoroughbred racing associations. The KHRA and the Kentucky Thoroughbred Development Fund Advisory Committee resolved the KTDF issue and put controls into place so that the fund is operated properly going forward.

- Launched a tamper resistant licensing card with a hologram to make duplication of the licenses practically impossible. Every licensee was required to obtain a new digital photo to update photos in the system and the use of the new card has thwarted attempts to copy or duplicate.
- Promoted horse racing and the KHRA to an expanded audience of Kentuckians. Deputy Executive Director Patricia Cooksey spoke to groups throughout the state including schools, legislative subcommittees, and many different business and civic groups to educate and lure more fans to horse racing in Kentucky.
- In the fall of 2006, John Veitch, Chief State Steward for thoroughbred racing, and Marc Guilfoil, Presiding Judge for standardbred racing began providing monthly reports to the Authority regarding the racing for the prior month. Included in these reports is a report on any rulings issued. Also in the fall, the KHRA began posting rulings on the KHRA Web site. In addition, Dr. Nancy Davis, Acting Chief State Veterinarian began reporting on the number of drug tests performed during the prior month.
- In October of 2006, the Equine Drug Research Council began discussing research proposals in Kentucky. One proposal involved the creation of a 20 horse stable that would be used to determine withdrawal times and threshold information for horses in training. The other proposal involved funding equipment and a full time pathologist at the UK Diagnostic Center to perform equine necropsies and other work.

These are just a few of our key accomplishments, and I am proud to announce that we made these achievements with one of the smallest regulatory racing staff in the nation.

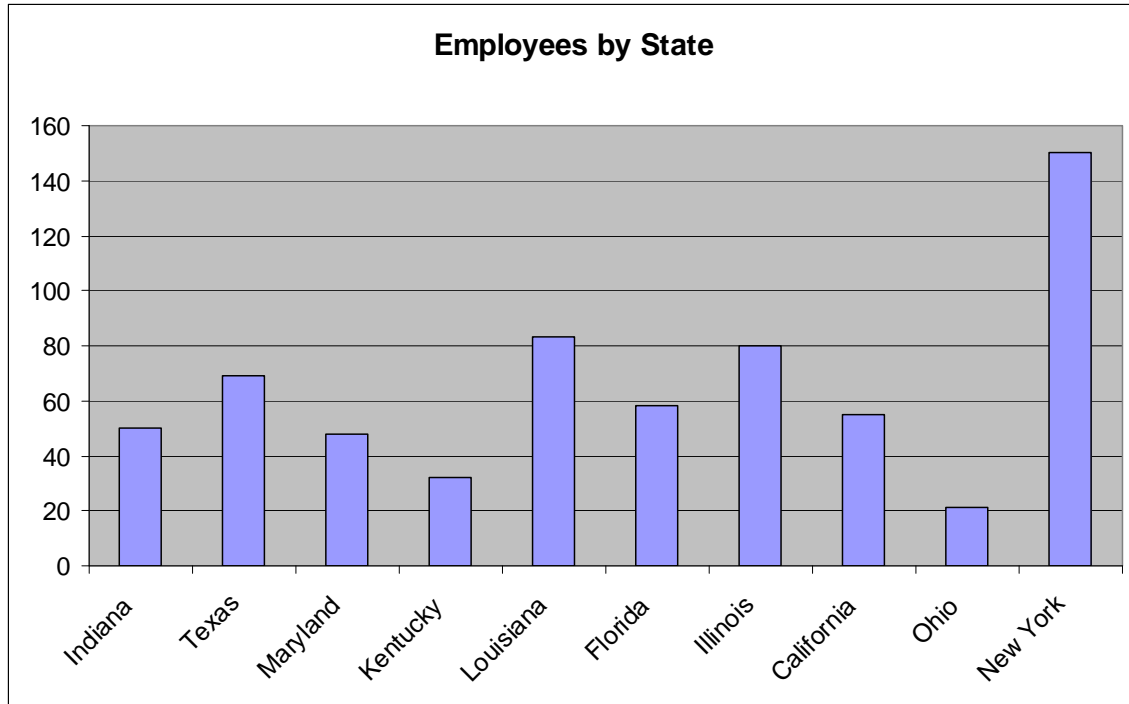
Also during 2006, the source of KHRA funding and staffing levels were analyzed by various constituencies. An internal review conducted by the KHRA early in 2006 had resulted in a recommendation to the Authority of a reorganization which would have created a Division of Incentive and Development and added positions such as the supervisor of pari-mutuel wagering and additional backside security personnel. The budget bill sent to the Governor by the legislature during the 2006 session provided that \$1.2 million of the KHRA budget normally funded through assessments to the racetracks

was to be replaced by general fund dollars during the 2006-2007 fiscal year. However, no replacement money was appropriated for the second year of the biennium.

The budget bill also required the auditor of Public Accounts to audit the Authority. This audit was conducted during 2006 and the report was issued in December 2006.

In summary, the auditor agreed with the conclusions reached internally by the KHRA—the KHRA is underfunded and inadequately staffed, as demonstrated by the graphic displayed below. Of the twelve states with the most active racing industry, Kentucky tied for last place in number of employees, and garnered tenth place in the amount of expenses incurred in regulating the racing industry. The information below is from the management audit prepared by the Kentucky Auditor of Public Accounts dated December 2006; however, the Kentucky number of employees has been modified to reflect the number of full-time employees, which is a more accurate description of the personnel in place as of December 31, 2006.

State	Expenses	Live Race Days	Employees
Indiana	\$2,294,284	251	50
Texas	\$4,762,989	312	69
Maryland	\$4,120,482	341	48
Kentucky	\$2,700,000	346	21
Louisiana	\$6,765,467	483	83
Florida	\$6,474,114	486	58
Michigan	\$3,505,976	492	Did not report
Illinois	\$6,825,000	694	80
California	\$8,747,000	950	55
Ohio	\$2,710,186	961	21
New York	\$14,052,000	1075	150



I am proud of the accomplishments we have made with the resources we have.

I thank our staff, our Board and our partners in the racing industry for working hard to achieve these successes.

We plan to continue this record of success in 2007. Topics on the forefront include:

- Securing adequate funding for the KHRA for the future.
- Securing appropriate staffing levels for the KHRA.
- Reviewing the use of digital fingerprinting by the Licensing Division.
- Hiring an Equine Medical Director to serve as the primary policy advisor on medication and drug testing issues impacting the Kentucky racing industry.
- Studying various projects for review by the Equine Drug Research Council.
- Reviewing different methods for monitoring the tote system.

Lisa E. Underwood
Executive Director, Kentucky Horse Racing Authority

ORGANIZATION AND 2006 KHRA ACCOMPLISHMENTS

I. STEWARDS AND JUDGES

The stewards and judges exercise immediate supervision, control and regulation of racing at each licensed race meeting on behalf of the Kentucky Horse Racing Authority. The powers of the stewards and judges include: authority over all horses and all persons, licensed or unlicensed, on association grounds during each race meeting as to all matters relating to racing and the determination of all questions, disputes, protests, complaints or objections concerning racing which arise during a race meeting. As a matter of course, Kentucky stewards review the films of each race from three different camera angles before the results are posted “official.” The Chief State Steward and the Presiding Judge are employees of the KHRA.

THOROUGHBRED RULINGS ISSUED DURING 2006	STANDARD BRED RULINGS ISSUED DURING 2006
Riding Infractions.....25	Driving Infractions..... 53
Entry or Procedure misconduct.....24	Causing late drivers change.....51
Medication Violations.....25	Medication Violations.....7
Unlicensed Participation.....3	Using Offensive/Profane Language to Officials.....2
Failure to Appear.....9	Late To Lasix.....5
Stable Area Violations.....8	Failure to honor Declaration.....3
Failure to Conduct Business Properly.....18	Failure to obey Paddock Judge.....1

II. VETERINARIANS

The Acting Chief State Veterinarian supervises the operations of the detention barn, the collection of urine and blood samples for testing and preparation and documentation of the urine and blood samples that are transported to the laboratory. The Acting Chief State Veterinarian also acts as the Authority's veterinary advisor for all medication issues.

The KHRA official veterinarians examine horses for soundness and racing fitness to ensure the health and safety of every horse and jockey. They maintain health records for all horses that compete at each race meet to compare previous injuries to each horse's present condition.

Authority veterinarians are present in the paddock, at the starting gate, in the test barn and on the horse ambulance during live racing in Kentucky. If a horse becomes unruly and injures itself, a KHRA veterinarian could recommend to the Chief State Steward or Chief State Judge that the injured horse be scratched from participating in the race for the protection, safety and health of every horse and rider.

Beginning July 19, 2006, the Authority veterinarians facilitated the performance of necropsies by the University of Kentucky Livestock Disease Diagnostic Center on horses that died or were euthanized as a result of a racing injury or related illness.

The KHRA detention barn technicians are responsible for the collection of post race equine urine samples to be sent to Iowa State Testing Laboratory for analysis. A strict "chain of command" protocol is carefully followed to ensure the integrity and honesty of each sample.

Kentucky's new medication withdrawal guidelines went into effect during 2006 to give horsemen and equine practitioners guidelines to follow as to when to withdraw certain therapeutic medications from a horse to ensure there will not be an overage or positive of a medication. This was the first published guidance of its kind in the United States.

In 2006 the Kentucky Veterinary Division collected a total of 5,638 urine samples and 6,395 blood samples to be tested for medication violations. In both standardbred and thoroughbred horses the winner plus one other horse was randomly chosen to have blood and urine samples taken for drug testing. Also in thoroughbred racing all graded stakes races were subject to TOBA testing, meaning the top four finishers are tested and the laboratory conducts tests for more medications. TCO₂ blood gas testing was conducted pre-race on a random basis to detect the level of carbon dioxide, a by-product of milkshaking, which neutralizes the buildup of lactic acid in a horses system. In thoroughbred racing TCO₂ testing is analyzed by the Iowa laboratory on a post race basis, while in standardbred racing TCO₂ testing is performed and analyzed pre-race on a random basis. There were 2,283 TCO₂ tests performed for thoroughbreds and approximately 1,280 standardbred TCO₂ tests conducted in 2006.

III. LICENSING

The Kentucky Horse Racing Authority requires all persons wishing to participate at Kentucky racetracks and facilities under the jurisdiction of the KHRA to be licensed.

The KHRA provided licensing services in all eight field offices during live racing meets and also at the main office located at the Kentucky Horse Park in Lexington, Kentucky.

A total of 20,894 licenses were issued by the five members of the licensing staff during 2006.

Each day the field licensing staff checked the racing program to ensure participants listed in the official program were licensed correctly and qualified to participate. The staff is trained in complex issues regarding multiple partnerships, racing syndicates, stable names, corporations and other matters concerning licensing in order to assist applicants.

In 2006 the licensing unit researched and designed a tamper resistant licensing card with a hologram to make duplication of the licenses practically impossible. Every licensee was required to obtain a new digital photo to update photos in the system and the use of the new card has thwarted attempts to copy or duplicate.

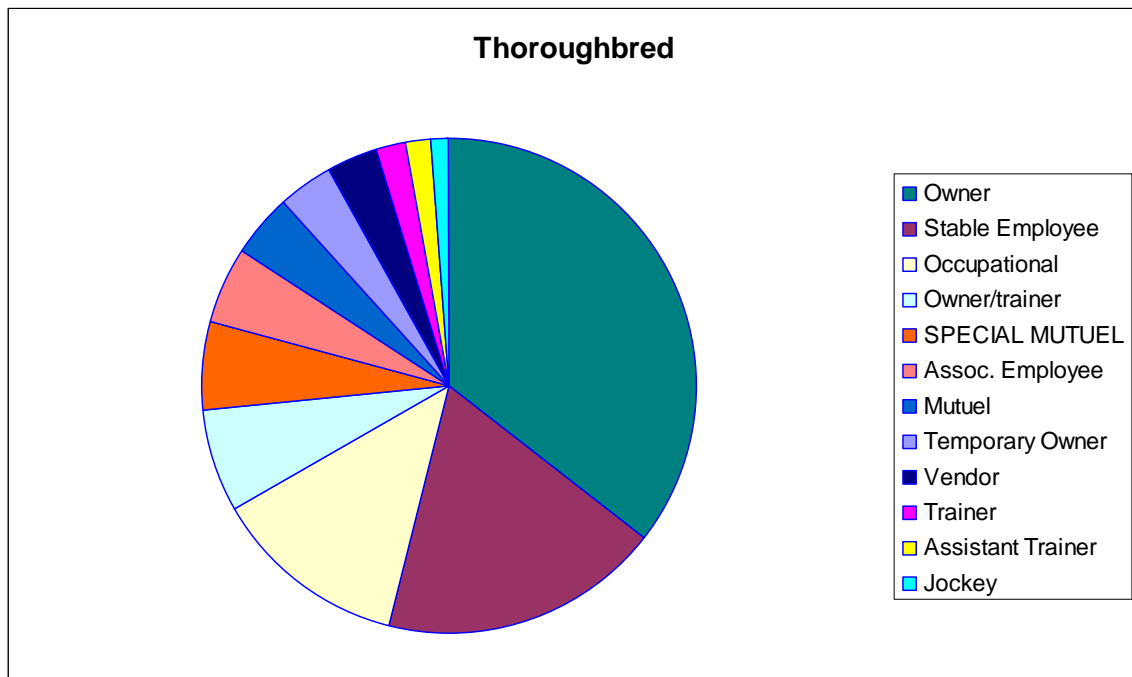
An improved filing system was implemented for better storage of applications.

License fee and cash handling protocols were refined to enhance the security of the collected funds.

Renewal applications were mailed to owners and trainers in the last quarter of 2006. Applications may also be downloaded from the KHRA Web site.

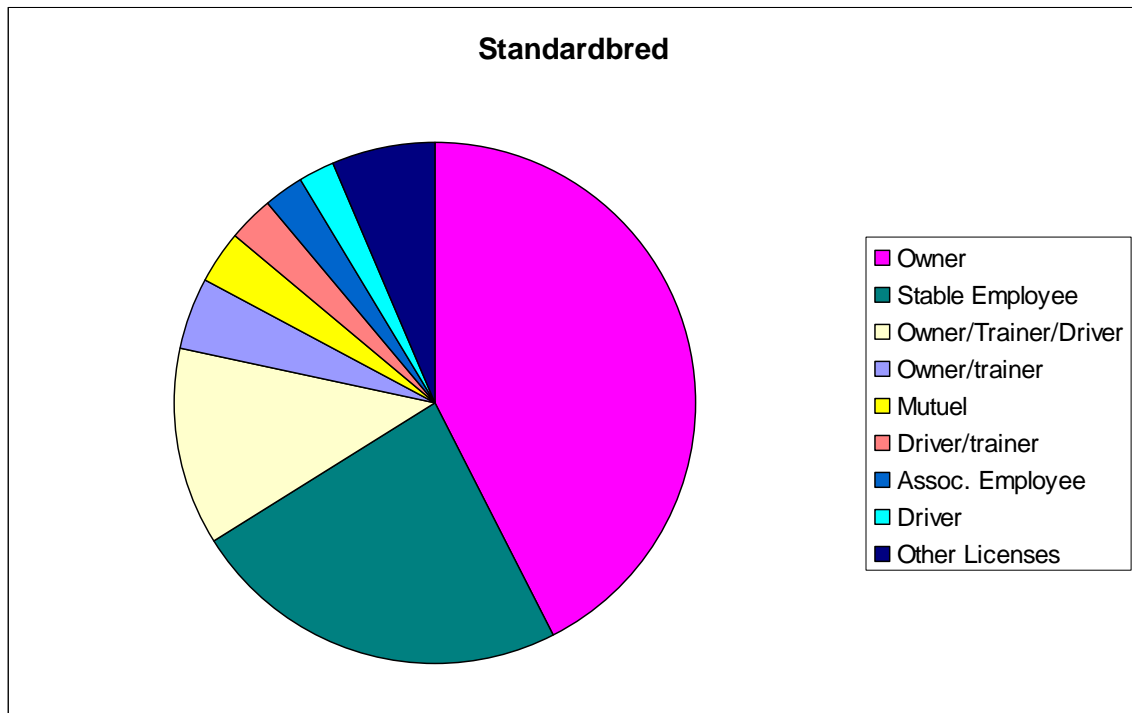
Thoroughbred Licenses issued 2006

License	Licenses Issued
Owner	6,253
Stable Employee	3,188
Occupational	2,239
Owner/trainer	1,151
SPECIAL MUTUEL	1,052
Assoc. Employee	878
Mutuel	712
Temporary Owner	622
Vendor	602
Trainer	328
Assistant Trainer	306
Jockey	197
Other Licenses	2,178
Total	19,706



Standardbred Licenses issued 2006

License	Licenses Issued
Owner	883
Stable Employee	487
Owner/Trainer/Driver	250
Owner/trainer	94
Mutuel	69
Driver/trainer	58
Assoc. Employee	49
Driver	48
Other Licenses	133
Total	1,188



IV. ENFORCEMENT

The primary duty of the Enforcement Division is to investigate and detect any violations of the laws as they pertain to thoroughbred, standardbred and quarter horse racing. The Enforcement Division is made up of a Director of Enforcement and one Investigator. The Enforcement Division conducts numerous investigational interviews with applicants who admitted to having criminal records and convictions for any public offense or a suspension of or revocation of a license for any racing related infraction.

The Division utilizes records and information from the Association of Racing Commissioners International (RCI), Thoroughbred Racing Protective Bureau (TRPB) and the KHRA database, as well as information from local police departments and the court systems, to gain information for criminal background checks and the suitability for licensure.

The Enforcement Division reviews documents supporting eligibility for employment of resident aliens and all foreign workers applying for licenses to prevent any problems between the applicant and the Immigration and Naturalization Service.

Potential or actual criminal offenses are investigated including human drug violations, assault on association grounds, burglary, theft, forgery and disorderly conduct. Investigations are also conducted regarding a vast array of other potential violations, such as hidden ownership, claims violations and pari-mutuel concerns. Barn searches are conducted as necessary.

The Enforcement Division works closely with local, state and Federal law enforcement agencies as well as with all security departments of racing associations under the jurisdiction of the Kentucky Horse Racing Authority. They constantly share intelligence information with all racing jurisdictions throughout the United States and Canada.

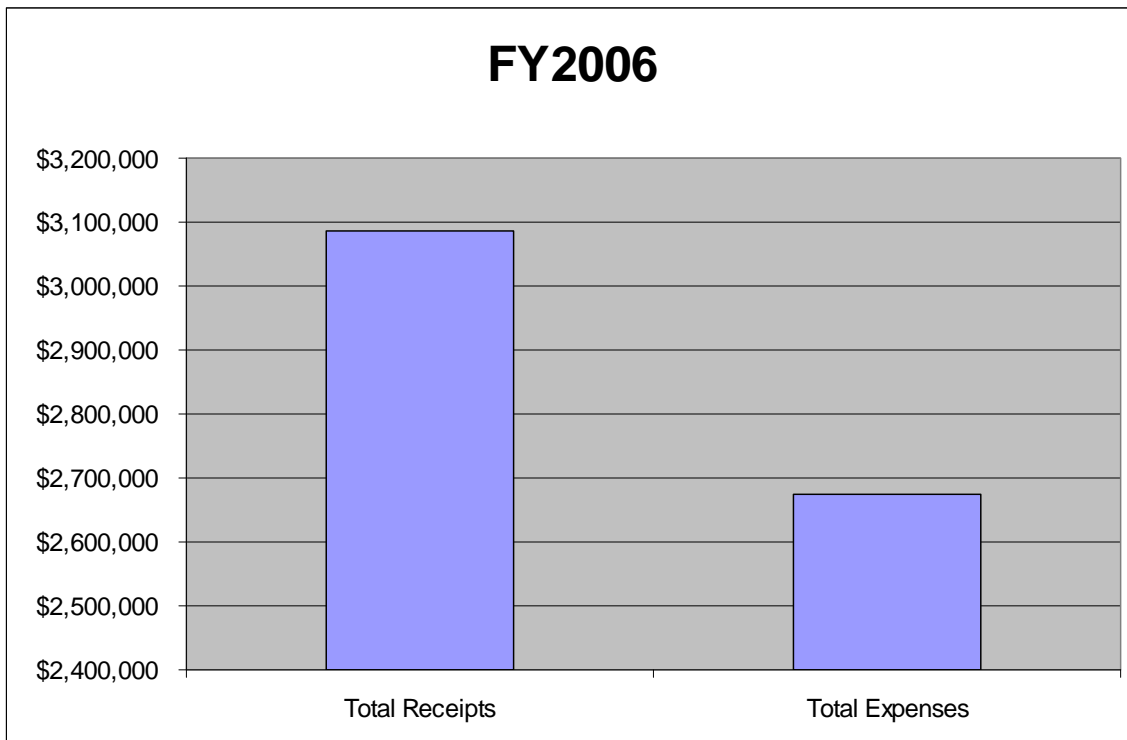
In an effort to maintain a constant flow of intelligence, the Director of Enforcement attended the annual meeting of the Organization of Racing Investigators (ORI) comprised of investigative staffs from all across the U.S. and Canada to share information and updates on all investigative matters concerning the racing industry. At the 2006 meeting the Kentucky Director of Enforcement, Mr. Jim Cain, was elected to the Board of Directors of the ORI as the representative for the Eastern Region.

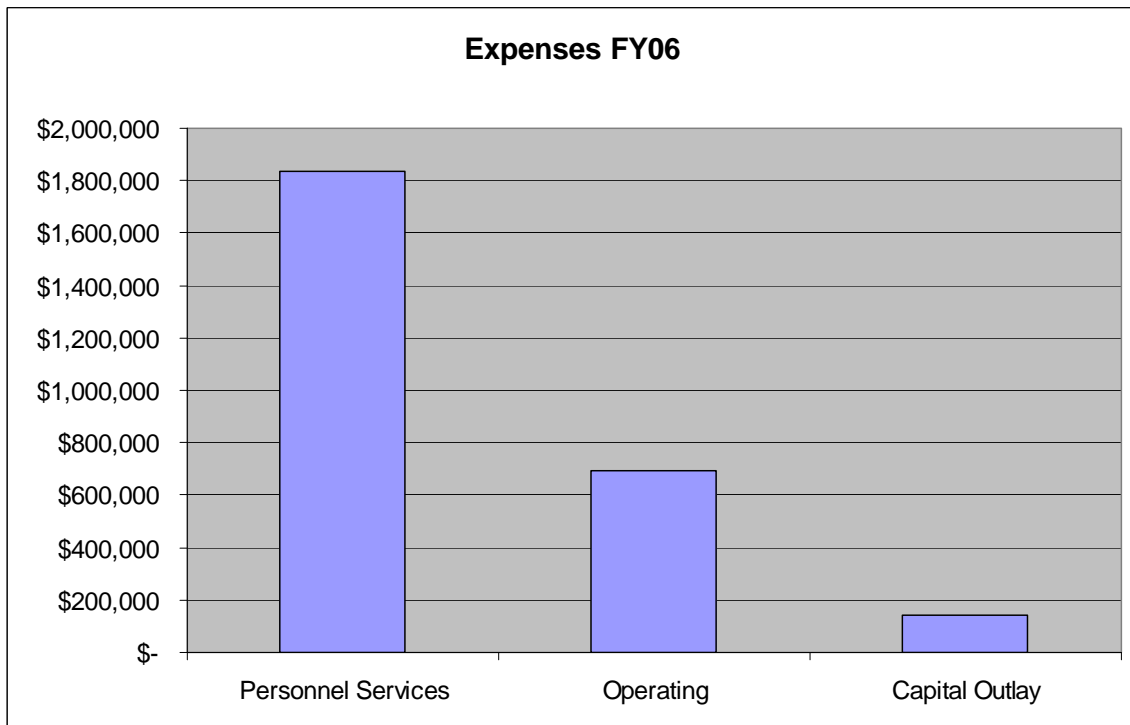
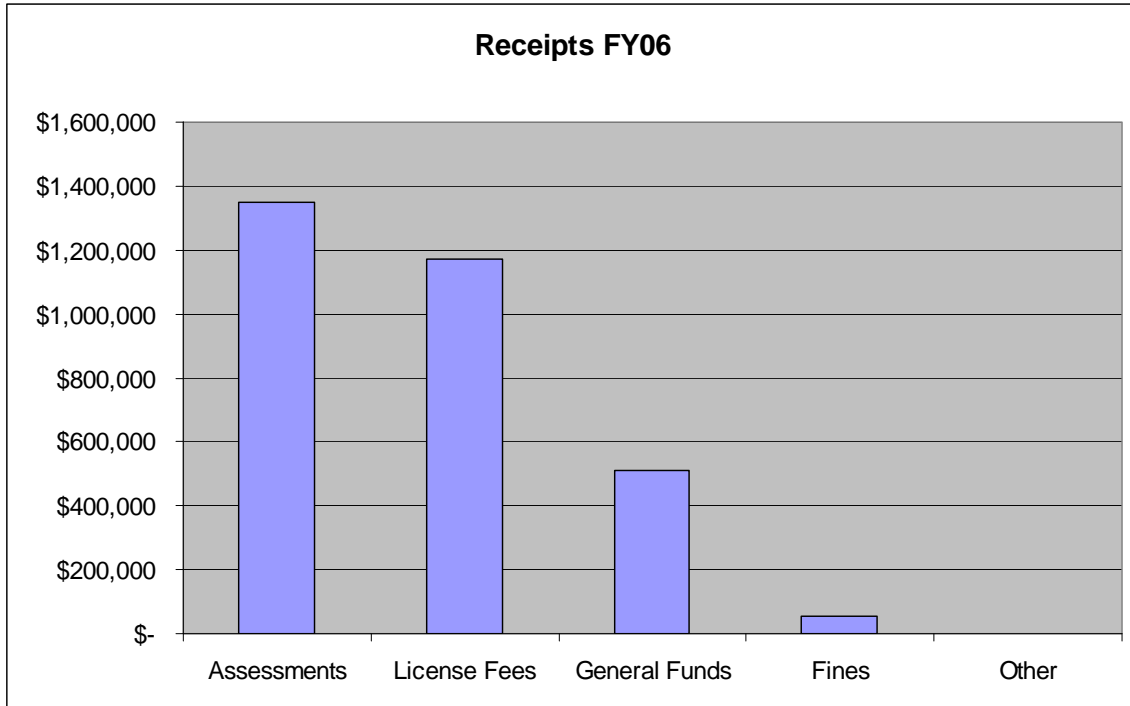
FINANCIAL OVERVIEW

This annual report is prepared for the 2006 calendar year. The Commonwealth operates on a fiscal year. The financial overview is presented on a fiscal year basis of July 1, 2005 through June 30, 2006.

Receipts	
Assessments	\$1,349,500
License Fees	\$1,171,287
General Funds	\$509,700
Fines	\$52,845
Other	\$2,226
Total Receipts	\$3,085,558

Expenses	
Personnel	\$1,836,181
Operating	\$695,117
Capital Outlay	\$142,350
Total Expenses	\$2,673,648





KHRA FUNDS

Among its other duties, the Authority is also charged with the oversight of several funds with specific purposes defined by statutes and regulations. For a description of the three different breeders' incentive funds, see "Kentucky Breeders' Incentive Funds." During 2006, the Kentucky Thoroughbred Breeders' Incentive Fund became operational and horses began earning awards. Also during 2006, the KHRA resolved a long standing discrepancy in the accounts relating to the Kentucky Thoroughbred Development Fund and entered into a Memorandum of Understanding to settle the accounts and provide procedures so there would be better accountability in the future. The KHRA is continuing to improve upon the procedures relating to the various funds and continues to administer these funds for the benefit of the regulated racing industry.

Below is a brief description of each of the funds:

Equine Drug Research Fund. The Equine Drug Research Council is a panel authorized by statute to advise the KHRA on the conduct of equine drug research and testing commissioned by the KHRA. The Equine Drug Research Fund is financed by one-tenth of one percent (0.1%) of the total amount wagered and subject to the pari-mutuel tax levied in KRS 138.510. Money from the Equine Drug Research Fund is to be used in financing drug research and testing research in Kentucky.

Health and Welfare Fund. The Kentucky Racing Health and Welfare Fund Inc. is an independent charitable corporation, organized for the benefit, aid, assistance and relief of thoroughbred owners, trainers, jockeys, valets, exercise riders, grooms, stable attendants, pari-mutuel clerks and other thoroughbred racing personnel employed in connection with racing, and their spouses and children, who can demonstrate their need for financial assistance connected with death, illness or off-the-job injury and are not otherwise covered by union health and welfare plans, workers' compensation, Social Security, public welfare or any type of health, medical, death or accident insurance. Proceeds from unclaimed pari-mutuel tickets provide the revenue for this fund.

Any reported pari-mutuel ticket that has not been claimed within one (1) year from the time the ticket became payable is presumed to be abandoned. Each year, any person or association holding any unclaimed tickets presumed abandoned as of July 1st of that year (in other words, any person holding on July 1st any tickets that have not, as of that date, been claimed for a year or more) is required to create a list of the tickets. The list, which records the amount of each ticket, is then submitted to the Authority by September 1st of the same year. Between November 1st and November 15th, the person or association then turns over to the Authority the sum represented by the tickets as reported.

In summary, the money turned over to the Health and Welfare Fund relates to pari-mutuel tickets that are over one year old. Specifically, the money given to the Health and Welfare Fund during 2006 relates to tickets that were originally sold to bettors between

July 1, 2004, and June 30, 2005, and were still unclaimed a year (or more) later on July 1st, 2006. The KHRA staff informally refers to these tickets as the “2006 tickets.” During 2006, the Health and Welfare Fund received \$2,329,197 from uncashed pari-mutuel tickets.

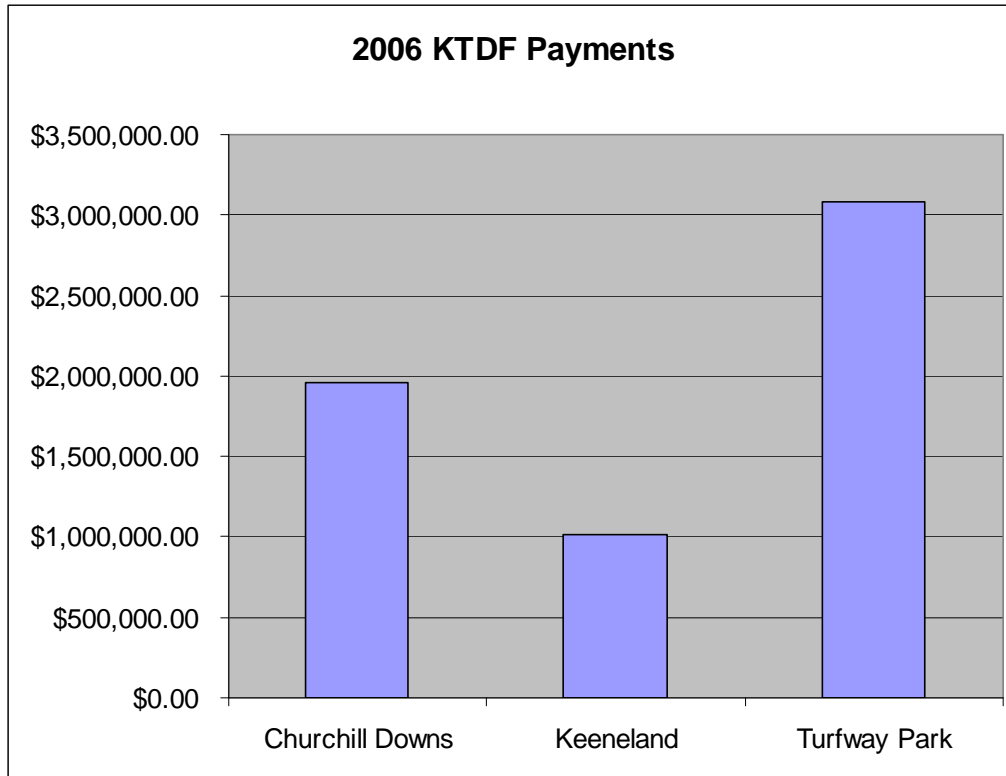
Kentucky Thoroughbred Development Fund (KTDF) Money from the KTDF is allocated to each licensed association in an amount equal to the amount the association contributed to the fund. This fund is used for purses and advertising. The KTDF receives .75% of all wagers from thoroughbred racetracks on live races and 2% of all wagers on simulcast races. It is an incentive program that seeks to encourage owners to buy from Kentucky markets, to board and breed mares on Kentucky farms, to mate them with Kentucky stallions, then to race the Kentucky-foaled horse at Kentucky tracks. This program was created in 1978 and placed under the general jurisdiction of the KHRA. A five-member Advisory Committee is appointed on July 1st of each year to advise and assist the KHRA with the implementation of this program. KTDF money supplements purses in stake, handicap, allowance and non-claiming maiden events in Kentucky. Only registered Kentucky-sired Kentucky-foaled horses are eligible to share in Fund purse supplements. Only the first four finishers participate, and on a basis of 65% to the winner, 20% to second, 10% to third and 5% to fourth.

KTDF 2006 PAYMENTS

Churchill Downs	\$1,958,212
Keeneland	\$1,018,187
Turfway Park	\$3,082,869

TOTAL \$6,059,269

As part of the memorandum of understanding Ellis Park did not receive funding from KTDF during 2006 due to past overpayment and Keeneland and Churchill Downs received a lower reimbursement.



Kentucky Standardbred Development Fund (KSDF) This fund was established to promote races, and to provide purses for races for horses sired by stallions standing within the Commonwealth of Kentucky. The fund is to be distributed to persons, corporations or associations operating licensed standardbred race tracks within Kentucky on an equitable basis, for the purpose of conducting separate races for two and three year old fillies and colts, both trotting and pacing, sired by standardbred stallions standing within the Commonwealth of Kentucky at the time of conception. The KSDF receives its revenue from the Kentucky Standardbred Breeders Incentive Fund (KYSBIF) and 1% of the total live handle of harness racing, 2% of all simulcast wagering and .70% of the 4% commission set aside for the County Fair Purse Fund. In FY 2006 \$205,000 was disbursed for purse supplements.

Standardbred Horseman's Fees. The Standardbred Horseman's account is financed from nominating payments and sustaining payments to the Horseman's account. These funds are used to supplement standardbred purses. In FY 2006 \$399,480 was disbursed for purse supplements.

County Fair Purse Fund. This fund is financed by money resulting from unclaimed standardbred pari-mutuel tickets and .30% of the 4% of the commission from the Off-Track Betting Parlors in Kentucky (OTB). In FY 2006 \$203,000 was disbursed for purse supplements.

Backside Improvement Fund. The purpose of the Backside Improvement Fund is to improve the backside of thoroughbred racing associations averaging \$1.2 million or less in pari-mutuel handle per racing day on live racing. It is funded by .5% of a track averaging less than \$1.2 million on track pari-mutuel wagers. Historically, Turfway and Ellis Park have been the associations participating in the Backside Improvement Fund.

Ellis Park received \$36,349 from the fund for new dormitories, paving roads in the stable area, installation of HVAC in dormitories and restrooms, painting dormitories and restrooms, and added 16 feed rooms to barns. Ellis Park still has an outstanding balance of \$211,696 related to these projects that will be paid off in future years as it earns the reimbursement amount.

Turfway Park received \$75,911 for projects related to the construction of a new guardhouse at the entrance of the backside, blacktop repairs and a manure management system in the receiving barn. Turfway Park still has an outstanding balance of \$42,902 related to these projects that will be paid off in future years.

Kentucky Thoroughbred Owners and Breeders Fund. Six percent (6%) of the commission on simulcast wagers from off-track betting (OTB) is allocated to the Kentucky Thoroughbred Owners and Breeders Inc., an independent Kentucky nonprofit corporation. This fund is required to be used for the following: Up to 3% for capital improvements and promotion of off-track betting and the remainder for marketing and promoting the Kentucky thoroughbred industry. In FY 2006 \$182,354 was disbursed for purse supplements.

KENTUCKY BREEDERS' INCENTIVE FUNDS

The Kentucky Breeders' Incentive Funds were implemented by Governor Ernie Fletcher as part of his Jobs for Kentucky plan. Included in the plan were tax incentives to ensure the strength and growth of the horse industry. The Breeders' Incentive Funds are financed through the 6% sales taxes paid on stallion stud fees. This is not a new tax. It is the same tax that has been required to be paid on stallion stud fees previously. Prior to the establishment of this Breeders' Incentive Fund, the stallion stud fee went into the General Fund of the Commonwealth – not back to the thoroughbred industry.

Kentucky Thoroughbred Breeders' Incentive Fund.(KBIF) The Kentucky Thoroughbred Breeders' Incentive Fund is financed from 80% of the receipts collected from the sales and use tax on the fees paid for breeding a stallion to a mare in Kentucky, together with any other money contributed, appropriated or allocated to the fund from all other sources. The money deposited in the Kentucky Thoroughbred Breeders' Incentive Fund is used to administer the fund and provide rewards for breeders of horses bred and foaled in Kentucky.

To qualify for the program, the mare must have been covered by a Kentucky stallion and remain in Kentucky from the time of cover until foaling. For each breeding season, the intended breeder of record is required to register the unborn foal with the KHRA before August 1 of the cover year, plus pay a filing fee of \$60 for each mare.

In 2006, the Thoroughbred Breeders' Incentive Fund paid awards to KY bred winners of horses racing in Kentucky in Maiden Special Weight (MSW), Allowance(ALW), Stakes Races and Grade I, II, and III, and in other states outside of Kentucky in MSW, ALW for two, three and four olds and Grade I, II and III. Awards are also paid in Grade I, II and III in Canada, England, Ireland and France.

For the first year of registration, approximately 11,200 mares were registered by Kentucky Thoroughbred breeders. Registrations can be made through the end of the yearling year so additional registrations for the 2006 breeding season are still arriving in the KHRA office and could continue up to December 31, 2008, for the 2006 breeding season.

Foals born in 2006 and prior years are grandfathered into the KBIF program if the foal is eligible for the KTDF. In 2006, Kentucky-bred horses won 3,989 races that qualified for incentives totaling \$12,654,845 to 1,789 Kentucky breeders for an average check of \$7,073 per breeder. The first Kentucky race which qualified under this new program was run at Turfway Park on January 1, 2006 and breeder James E. Nelson received a check for \$4,691 for "On the Border's" win.

Kentucky Standardbred Breeders' Incentive Fund(KYSBIF) The Kentucky Standardbred Breeders' Incentive Fund is financed from percent 13% of all receipts collected from the sales and use tax on the fees paid for breeding a stallion to a mare in Kentucky, together with any other money contributed, appropriated, or allocated to the fund from all other sources. The money deposited in the Kentucky Standardbred Breeders' Incentive Fund is used to administer the fund and provide rewards for breeders or owners of Kentucky-bred standardbred horses through the KSDF. Due to the breeders' awards received by the standardbred industry, six stallions have been relocated to Kentucky farms as a direct result of the incentive program.

Valley Victor, a five-time leading sire in Illinois has changed residency to Kentucky. The presence of these top sires has helped revitalize Kentucky's harness industry which has struggled in recent years.

Kentucky Horse Breeders' Incentive Fund(KHBIF) The non-race breeds are rewarded under the Kentucky Horse Breeders' Incentive Fund from 7% of all receipts collected from the sales and use tax on the fees paid for breeding a stallion to a mare in Kentucky, together with any other money contributed, appropriated or allocated to the fund from all other sources. The money deposited in the KHBIF is used to administer the fund and provide rewards for breeders of horses bred and foaled in Kentucky. On Monday, April 16, 2007, the Kentucky Horse Racing Authority, on the recommendation of the Horse Breeders' Incentive Fund Advisory Committee, approved nine applications for the fund. This application period will cover the years 2006, 2007 and 2008.

For the 12-month collection period of July 1, 2005, through June 30, 2006, the Department of Revenue collected and transferred \$1,131,706 to the KHBIF account. These monies will account for the 2006 calendar year awards for this fund.

<u>Kentucky Affiliates</u>	<u>Incentive Funds</u>
KENTUCKY APPALOOSA OWNERS ASSOCIATION	\$50,861
SOUTH CENTRAL HACKNEY ASSOCIATION	\$13,554
KENTUCKY MORGAN HORSE ASSOCIATION	\$13,937
KENTUCKY MOUNTAIN HORSE	\$136,447
KENTUCKY PAINT HORSE CLUB	\$95,263
KENTUCKY PASO FINO HORSE ASSOCIATION	\$11,680
KENTUCKY QUARTER HORSE ASSOCIATION	\$368,942
KENTUCKY SADDLEBRED OWNERS AND BREEDERS ASSOCIATION	\$120,919
KENTUCKY WALKING HORSE ASSOCIATION	\$320,103
TOTAL	\$1,131,706

KENTUCKY 2006 RACING HIGHLIGHTS

- Turfway Park, the first track in North America to run over a synthetic surface, showed substantial gains in handle both on and off track for its winter/spring meet.
- Turfway's 22-day fall meet ended with double-digit increases in off-track and all sources of mutuel handle, an increase of 23.6% over the 2005 fall meet.
- During the 2006 Keeneland Spring meet, average daily attendance and total attendance records were set.
- A single day attendance record also fell on April 14, 2006, at Keeneland when 23,882 fans watched a great day of racing.
- The 17-day Keeneland 2006 Fall meet set all-time records for all-sources handle while racing over the synthetic Polytrack surface for the first time.
- The Trakus technology system was used for the first time at Keeneland to track horses during the running of each race and displayed on a giant screen.
- Wagering records were set on the 2006 Kentucky Oaks with a 43% increase over 2005 Oaks Day.
- Louisville-based Yum! Brands Inc. became the first-ever presenting sponsor of the \$2 million Kentucky Derby.
- The North American record for wagering on a single race was shattered when total wagering on the 2006 Kentucky Derby, which includes on-track and simulcast betting, soared to over \$118 million.
- A record \$10 million in stakes purse money was offered during the Churchill Downs Spring/Fall meets with a total of 47 stakes races.
- The Breeder's Cup World Championships made a record sixth appearance at Churchill Downs on November 4, 2006.
- Ellis Park saw gains in average daily on-track wagering and attendance.
- Four track records were broken during the Ellis Park meet.

- Apprentice jockey Julien Leparoux set several new records over the course of 2006. He set a new winter-spring record at the Turfway meet with 167 wins from 529 mounts, a win rate of 32%. He also set his second record at the Turfway Park Fall meet with 38 wins, tumbling a 38-year record.
- In addition, Mr. Leparoux became the first apprentice jockey to win a leading rider title at the Keeneland Spring meet when he tied with Rafael Bejarano for leading jockey honors. Mr. Leparoux won the Churchill Downs Spring meet title and became the first apprentice jockey to win a Downs riding crown since 1949.
- In the standardbred circuit, two-year olds raced for three \$50,000 legs and a \$200,000 final for the first time ever in the Kentucky Sire Stakes. In 2007, the success will continue with three year-olds when the stage is set for a Kentucky Super Night of racing where all eight divisional championships will compete for over \$500,000!
- The Red Mile was named “The Track of the Century” by the United States Trotting Association.
- The Kentucky Filly Futurity required a dramatic two-horse, three heat match race to determine the winner. National attention was focused on the sport of harness racing when driver Ron Pierce, driving eventual winner, “Passionate Glide” waved “goodbye” to Trond Smedshammer and “Queen Serene” as he passed them in the stretch on the way to victory.
- The second jewel of the Trotting Triple Crown saw a stunning win by three year-old colt “Glidemaster” as his driver said the win was redemption after Glidemaster had run off during the post parade of the 2005 Futurity, ruining his chances for victory that year.

Total Pari-Mutuel Wagering 2006

Track	Live	Intertrack	Track Handle on Imported Out of State Signals	Out of State Handle bet on KY Races	On Track Handle	Total Bet on KY Racing	Total Wagers at Track
Churchill Downs	\$104,853,782	\$15,903,918	\$70,701,726	\$669,516,158	\$120,757,700	\$790,273,858	\$191,459,426
Keeneland	\$42,805,814	\$19,383,889	\$61,090,687	\$219,312,412	\$62,189,704	\$281,502,116	\$123,280,390
Turfway	\$15,558,289	\$8,391,695	\$42,636,558	\$309,378,001	\$23,949,984	\$333,327,985	\$66,586,542
Ellis Park	\$7,269,900	\$6,845,739	\$19,702,772	\$79,272,508	\$14,115,639	\$93,388,147	\$33,818,411
Kentucky Downs	\$366,712	\$5,021,726	\$21,134,975	\$7,830,510	\$5,388,438	\$13,218,948	\$26,523,413
Red Mile	\$2,463,273	\$0	\$34,249,904	\$13,656,235	\$2,463,273	\$16,119,507	\$36,713,177
Players Bluegrass	\$96,573	\$1,614,985	\$4,849,717	\$0	\$1,711,558	\$1,711,558	\$6,561,275
Thunder Ridge	\$20,736	\$1,374,020	\$4,864,642	\$0	\$1,394,756	\$1,394,756	\$6,259,398
Totals	\$173,435,078	\$58,535,972	\$259,230,981	\$1,298,965,824	\$231,971,051	\$1,530,936,875	\$491,202,032

KENTUCKY HORSE RACING AUTHORITY COMMITTEES

The Kentucky Horse Racing Authority met 12 times during 2006. Meetings of the KHRA are open to the public. In addition, Chairman Street appointed several committees which met throughout the year as needed. The committees for 2006 were as follows:

Rules Committee- This committee reviewed the regulatory structure of the KHRA and made recommendations on regulations regarding the racing industry.

Tom Handy, Chairman

Douglas Hendrickson

Larry Telle

Ben Walden

Connie Whitfield

Cumberland Downs New Track Application Committee- This committee was charged with analyzing the application to establish a new race track facility at Cumberland Downs in Whitley County.

John Cashman, Chairman

Dell Hancock

Thomas Handy

Douglas Hendrickson

Thoroughbred Breeders' Incentive Fund Committee- This committee made recommendations to the Authority regarding the structure and operation of the thoroughbred breeders' incentive fund.

Douglas Hendrickson, Chairman

Kerry Cauthen

Thomas Gaines

Dell Hancock

Ben Walden

In addition there are two other committees on which KHRA members serve that are connected to the KHRA:

Kentucky Thoroughbred Development Fund Advisory Committee- This committee advised and assisted the KHRA in the development of the supplemental purse program funded by a portion of the pari-mutuel tax to Kentucky thoroughbred racetracks to enhance purses paid on Kentucky races.

Dr. David Richardson, Chairman

Douglas Hendrickson

W.R. Rogers Beasley

William Landes

Pete Salmen

Equine Drug Research Council- This committee made recommendations to the KHRA regarding equine racing medication rules and policies.

Connie Whitfield, Chairman

Dr. Fairfield Bain

Susan Bunning

Alice Chandler

Dr. Gary Lavin

Alan Leavitt

William Napier

Senator Damon Thayer

John Ward

KENTUCKY HORSE RACING AUTHORITY SENIOR STAFF

Executive Director Lisa E. Underwood was appointed by Governor Ernie Fletcher in October 2006. Prior to her appointment, Ms. Underwood served the administration as Deputy Commissioner of the Department of Public Protection and as acting general counsel for the KHRA. Prior to joining state government, Ms. Underwood served as a partner in the law firm of Wyatt, Tarrant and Combs, PLLC and as senior counsel for Mason and Hanger Company.

Jim Gallagher served as Executive Director of the KHRA during 2006 until early October when Ms. Underwood was appointed. Mr. Gallagher formerly served in a variety of positions for the New York Racing Commission.

Patricia J. Cooksey served as Deputy Executive Director, bringing many years of experience in the racing industry to the Authority. She is currently the second winningest female jockey in the history of thoroughbred racing and holds the record for most wins by a woman jockey at historic Churchill Downs. She was appointed by Governor Fletcher in September 2005 to promote the racing industry in Kentucky and nationally.

Marc Guilfoil served as Director of Standardbred racing and oversaw the regulation of Kentucky's Standardbred Racing Industry. For the past 21 years, Mr. Guilfoil acted as Presiding Judge for the standardbred meets in Kentucky. He was also director of the Standardbred Development Fund.

Mr. John Veitch served as Kentucky's Chief State Steward and oversaw the thoroughbred racing industry at live racing meets in Kentucky. Mr. Veitch has been a longtime horseman and trainer and during 2007 was elected into the Racing Hall of Fame. He trained Alydar, whose rivalry with Triple Crown Winner Affirmed, is legendary.

Jamie Haydon administered the new Breeders' Incentive Funds. Mr. Haydon has also been tasked with implementing changes in the operations of the Kentucky Thoroughbred Development Fund, the Kentucky Standardbred Development Fund, the Kentucky Horse Development Fund, the Backside Improvement Fund and the Health and Welfare Fund. Mr. Haydon previously served as Director of Sales with Four Star Sales LLC.

John Forgy is a former Kentucky State Prosecutor, who became the general counsel of the Department of Public Protection in June 2004. He now serves as general counsel for the KHRA.

Dr. Nancy Davis served as the Acting Chief State Veterinarian. After more than 30 years with the Kentucky horse racing industry, Ms. Davis retired from the KHRA April 27, 2007, at the conclusion of the Keeneland Spring meet.

Jim Cain served as the Director of Enforcement and has performed this function since April 2000. Mr. Cain oversaw investigations of administrative and criminal statutes as they pertained to the horse racing industry in Kentucky. Jim is a retired Lieutenant Colonel of law enforcement with the Jefferson County Sheriff's Department and brings over 25 years of investigative and management experience to the KHRA.