



BOARDWORKS
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New Zealand Racing Board

Performance and Efficiency Audit

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Executive Summary

Under the Racing Act 2003 the New Zealand Racing Board ('the NZRB') must arrange for an audit to be conducted in relation to how effectively and efficiently it is performing its statutory functions at least once every 5 years. This first such audit under the 2003 Act examines:

- the extent to which NZRB has established objectives for the performance of its functions;
- the nature of those objectives;
- the progress NZRB is making towards the achievement of those objectives;
- the extent to which NZRB has put in place policies and strategies to use its resources effectively and efficiently for the purpose of achieving those objectives; and
- the nature of those policies and strategies, and the manner in which they were put in place.

The focus of the audit has been primarily at the governance level of the organisation where the ultimate accountability for the NZRB's performance lies. It also examines the way in which strategies and policies determined or approved at the governance level are cascaded to, and by, senior management and how the NZRB relates to the three racing codes.

The audit has concluded that the NZRB has achieved much since its formation and it has many further initiatives 'on the boil'. For example, as a consequence of steps taken by the NZRB, the industry is far better informed about its essential characteristics (including its basic economics) than it was five years ago. Although there are 'structural' tensions, relationships within the industry (e.g. between the NZRB and the racing Codes) have improved significantly and there is greater transparency of information. The NZRB has adopted a disciplined, evidence-based approach to the changes it has pursued. Not least the NZRB has made major financial gains for the industry which are significant even when the effect of advantageous tax changes is excluded.

Key stakeholders like the Codes are generally positive about the progress the NZRB has made, particularly in a financial sense. There is a broad understanding of the reasons why more progress might not have been made in some areas but also some frustration.

The NZRB is still a relatively young organisation. It is an industry 'peak body' that operates in a comparatively fragmented and internally competitive institutional environment. In addition, the organisation, and the industry as a whole, operates in a dynamic global environment. Some of its functions face intense competition. Consequently, the status quo is not an option. The organisation, in conjunction with the wider industry, must 'get better, faster'. While both governance and management performance have been progressively strengthened during the first five years of the NZRB's existence, there must continue to be a significant premium placed on good governance and management.

While it concludes that many of the organisation's basic governance and management systems are working well and producing good results the report also identifies areas where

further development and strengthening are desirable. Initiatives suggested are in the nature of ‘progressive incremental improvements’ rather than matters requiring ‘urgent remedial attention’.

In particular, the NZRB’s articulation of its strategic intent and strategic direction requires further development. Process improvements are also possible and desirable particularly where these draw other key stakeholders into a productive on-going strategic dialogue. Such improvements as have been canvassed in the report would not only produce gains in transparency and accountability but would be important initiatives towards the integration, cohesion and performance of the industry.

1 Introduction to the Audit

1.1 *The Effectiveness and Efficiency Audit*

The Racing Act 2003 (‘the Act’) requires that, at least once every 5 years, the New Zealand Racing Board (‘the NZRB’) must arrange for an audit to be conducted in relation to how effectively and efficiently it is performing its statutory functions.¹

As required by the Act, the NZRB consulted recognised industry organisations in the preparation of the Terms of Reference for the audit. The full Terms of Reference are attached (Appendix 1).

Graeme Nahkies, Director of BoardWorks International (NZ) Ltd (‘the Auditor’) was appointed by the NZRB to undertake the audit and is the author of this report. In summary, the auditor was required to consider:

1. the extent to which NZRB has established objectives for the performance of its functions;
2. the nature of those objectives;
3. the progress NZRB is making towards the achievement of those objectives;
4. the extent to which NZRB has put in place policies and strategies to use its resources effectively and efficiently for the purpose of achieving those objectives;
5. the nature of those policies and strategies, and the manner in which they were put in place; and
6. any other matters determined by NZRB.

The audit is intended to examine, verify and, if appropriate, validate, the steps the NZRB has taken to date in relation to these matters and to recommend any further steps the NZRB should take to ensure that it is well positioned and capable of discharging its functions.

To address these Terms of Reference, the approach adopted has been to describe, verify and evaluate the steps the NZRB has taken to date in respect of:

1. the structures and processes adopted by the NZRB to enable it to conduct its affairs in an efficient and effective manner (including, for example, an examination of governance structures and processes);
2. the process by which the NZRB has established objectives for the performance of its functions (in essence, how the Board has gone about the articulation of its purpose and functions and the determination of its priorities);
3. the nature and content of policies and strategies intended to achieve the objectives (for example, assessing whether policies, strategies and decision making criteria (including statutory requirements) appear reasonable and are in alignment with the objectives they are intended to achieve);

¹ Section 14, Schedule 2 (1)

4. the framework for delegation to those responsible for implementation (assessing whether policies and strategies set by the NZRB have been communicated and delegated to management in a manner that clarifies accountability, and facilitates effective implementation, including the management of risk);
5. the process and a framework for monitoring implementation of strategies and policies (assessing whether the board² has a process and an effective and efficient monitoring system for ensuring that policies and strategies are implemented as intended and, to the extent that they are/are not efficient and effective, there is an appropriate feedback loop resulting in necessary improvements).

While the focus of the audit has been primarily at the governance level of the organisation where the ultimate accountability for the NZRB's performance lies, the Auditor has examined the way in which strategies and policies determined or approved at the governance level are cascaded to, and by, senior management and how the NZRB relates to the three racing codes.

To reach conclusions on these various matters the Auditor has relied primarily on an examination of the NZRB's documentation of the various steps it has taken to discharge its responsibilities in relation to each of its defined functions. To this end the auditor has examined:

- Racing Board agendas, minutes and associated meeting papers, including executive reports to the board.
- Other relevant documentation including major strategic and business planning documents, policies, instruments of delegation, monitoring, etc.

To further explore issues raised in the Terms of Reference and to verify matters arising from the review of documentation, the Auditor has interviewed a number of NZRB-related personnel and stakeholder (principally Code) representatives (see Appendix 2). It should be noted, however, that this audit was not conceptualised as a consultative exercise and has not been conducted as such.

An initial draft of this report was made available to the NZRB to verify factual material and the Auditor's understanding of the way in which particular NZRB-led initiatives have proceeded. This was discussed both with senior management and, separately, with members of the board. All matters of interpretation and judgement remaining in this report remain the responsibility of the Auditor.

In addition to the conclusions reached about the way the NZRB has gone about its functions, a range of recommendations have been formulated. The principal recommendations are numbered, highlighted in the text and summarised in the final part of the report.

² Given the scope and nature of the audit, much of the review process has required a focus on the leadership and actions of the governing board of NZRB, hereafter referred to as 'the board'.

NZRB and wider industry personnel approached for assistance, information or to discuss matters related to this audit, often at short notice, have been unstintingly cooperative and open. Their involvement is greatly appreciated.

1.2 The Establishment of the New Zealand Racing Board

After the passage of the Act, the NZRB was established on 1 August 2003. The intent of the new legislation, which replaced the 1971 Racing Act, was to provide a simplified and more efficient framework for New Zealand racing. The Act:

- disestablished the Racing Industry Board and the TAB;
- established the NZRB as the industry's principal policy body and as the provider of race and sports betting services (the TAB brand and its operations continued under the New Zealand Racing Board);
- gave the three racing codes (thoroughbred, harness and greyhound) increased responsibilities, especially around expenditure and governance arrangements;
- strengthened the accountability arrangements for industry bodies, including deeming the rules of racing to be regulations;
- required the NZRB to distribute betting profits to the three racing code bodies for onward distribution to their constituent racing clubs; and
- maintained horse racing's statutory judicial system managed by the Judicial Control Authority (greyhound racing has its own judicial system).³

As stated in the Act, the objectives of the NZRB are:

- To promote the racing industry;
- To facilitate and promote race betting and sports betting;
- To maximise its profits for the long-term benefit of New Zealand racing.

Another important starting point for an examination of the NZRB's performance and efficiency is its statutory functions. These are defined in the Act (Section 9.1) as follows:

- (a) To develop policies that are conducive to the overall economic development of the racing industry, and the economic well-being of people who, and organisations which, derive their livelihoods from racing.
- (b) To determine the racing calendar each year, and issue betting licenses, under Part 5.
- (c) To conduct racing betting and sports betting, and make rules relating to betting, under Part 6.
- (d) To distribute funds obtained from betting to the racing codes in accordance with sections 16 and 17.
- (e) To administer the racing judicial system in accordance with sections 36 to 41 and Schedule 3.

³ Source: Department of Internal Affairs briefing for the Incoming Minister of Racing, 2005

- (f) To develop or implement, or arrange for the development or implementation of, programmes for the purposes of reducing problem gambling and minimising the effects of that gambling.
- (g) To undertake, or arrange for the undertaking of, research, development, and education for the benefit of New Zealand racing.
- (h) To use its resources, including financial, technical, physical, and human resources, for purposes that, in the opinion of the Board, will directly or indirectly benefit New Zealand racing.
- (i) To keep under review all aspects of racing and to advise the Minister of those aspects, either on its own initiative or at the request of the Minister.
- (j) Any other functions that it is given by or under this Act or any other Act.

In carrying out these functions, the Board must also:

- Comply with the principles of natural justice.
- Exhibit a sense of social responsibility by having regard to the interests of the community in which it operates.⁴

1.3 Other Important Components in the Industry Governance Structure

The two other principal components in the industry governance structure are the racing codes and the various local racing clubs. The governing bodies of the three racing codes are New Zealand Thoroughbred Racing, Harness Racing New Zealand and the New Zealand Greyhound Racing Association. The racing code bodies are sometimes referred to as the 'racing conferences' because they are associations of racing clubs that meet at an annual conference. The code bodies are responsible for the rules of racing, and for the licensing and registration of all racing participants (e.g. horses, greyhounds, trainers, breeders, jockeys, drivers etc.).

The racing clubs promote, conduct and control race meetings in accordance with the relevant rules of racing. They are mostly incorporated societies. There are approximately 70 thoroughbred racing clubs, 50 harness racing clubs and 12 greyhound racing clubs currently holding licences to conduct totalisator race meetings.

An attempt has been made by the NZRB to summarise the broad mix of roles and responsibilities between the NZRB, the racing codes and the clubs (see Appendix 3).

In addition, the Act recognises the following sector groups:

- New Zealand Racehorse Owners' Federation
- New Zealand Thoroughbred Breeders' Association
- New Zealand Trainers' Association
- New Zealand Jockeys' Association

⁴ Section 9 (2)

- New Zealand Standardbred Breeders' Association
- New Zealand Harness Racing 'Trainers' and Drivers' Association
- New Zealand Trotting Owners' Association.

Including the NZRB, the codes, the clubs, and these sector groups, the Act gives recognition to over 140 'Recognised Industry Organisations'.

1.4 The Extent of the Industry

The racing industry is a major feature of New Zealand's economic and social landscape. In economic terms a 2004 IER study⁵ commissioned by the NZRB estimated, at that time, that:

- The racing industry made a direct contribution of \$424 million to New Zealand's GDP (0.37% of total GDP), and it generated more than \$1,480 million (1.3% of GDP) if the indirect impact of expenditure in the racing industry was taken into account.
- More than 40,000 people were involved in some capacity in the racing industry (74% in the production of racing animals (breeding, training etc) and 26% in racing club, raceday and TAB operations). The racing industry directly sustained 9,248 full-time equivalent (FTE) jobs, and when the indirect impact of racing on other industries was taken into account, the total employment impact increased to 18,320 FTE jobs.
- The racing industry generated more than \$130 million in annual export sales of thoroughbred and standardbred horses (primarily to Australia followed by Asia). Approximately 1,900 thoroughbreds were exported each year.

In social terms, the IER study found that the New Zealand racing industry made a significant contribution to community social benefit. It identified that more than 150 racedays have a community leisure theme, and many racing clubs share their facilities with community organisations on non-racedays for activities such as fairs, expos, car rallies, craft and agricultural shows, and pony clubs. There were more than 27,000 members of racing clubs nationwide, and a high level of voluntary work within the racing industry (IER estimated that 3,916 volunteers were participating in racing clubs).

Notwithstanding the size and importance of the industry, racing in New Zealand is almost entirely dependent on gambling for its continued viability with betting profits being distributed through the code bodies to racing clubs. However, taking inflation into account, gambling expenditure on racing industry products declined by about 25% between 1989 and 2005.⁶

Because of its importance in so many different ways, the effectiveness and efficiency of the NZRB has great significance not only for racing industry participants, but for New Zealand generally.

⁵ Size & Scope of New Zealand Racing Industry, Institute of Economic Research, June 2004

⁶ Department of Internal Affairs briefing for the Incoming Minister of Racing, 2005

2 Achievements to Date

2.1 Introduction

To create a context for the subsequent analysis, this Part examines the extent of progress made by the NZRB since its establishment, to confront the challenges facing the racing industry.

2.2 Principal NZRB Initiatives to Advance the Industry 2003-2008

In a presentation to the industry in September 2004, the then Chairman of the NZRB advised that the status quo in the industry was not sustainable. He stated that the successful implementation of the NZRB's strategy could produce between \$20m and \$35m with up to \$15m of that coming from the NZRB and the balance from the industry. Central to the NZRB's strategy was the 'Pathway to \$100m'.⁷

A review of NZRB board papers since its formation shows that the focus of the NZRB since its formation has constantly been on the need to bring about change. It is beyond the scope of this audit to determine whether the change achieved has been either adequate or sufficient. Clearly, however, much *has* been achieved since the NZRB's formation. Culled from a range of sources⁸, the following initiatives and achievements appear to have been significant during the first five years of the NZRB's existence.

- Completion of a major economic study on the New Zealand racing industry (IER). This early initiative provided an important fact base, to overcome the historic reliance on anecdotal evidence. It also gave the stakeholders (including the Government) a real measure of the economic importance of the industry.
- Completion of a performance and efficiency review (BCG). This study provided insights into areas of potential performance gain and was the foundation on which the NZRB's initial business planning was based.
- The appointment of a chief executive and an overall strengthening of the senior management team. Subsequently, the appointment of a Legal and Risk team.
- The shift of New Zealand Thoroughbred Racing (NZTR) to the NZRB National Office site at Petone. The co-location of key operational staff of the Board and the largest Code has made faster progress possible.
- The initiation of cultural change throughout the NZRB. Some entrenched territorial/patch attitudes were inevitably brought forward from the antecedent organisations. Higher minimum standards operationally and behaviourally have been set.

⁷ W. Larsen. Where To From Here for the Industry. Presentation to the Racing Industry, 14, 21 September 2004

⁸ Annual reports, communications with NZRB and Code representatives.

- Resolution of the taxation anomaly. A board committee produced in-depth analyses which proved the case for tax and duty re-alignments. This work became the basis for the Racing Minister's tax package which has made a significant financial contribution to industry performance since its introduction.
- A range of proactive steps to minimise the harm of problem gambling. In 2007/08 over 100 potential problem gambling incidents were investigated resulting in 37 customer exclusion notices being issued. A further seven account customers were placed on the Set Your Limits betting exclusion programme. Work is under way to develop a predictive model of problem gambler risk to assist in the early identification of customers who may be moving into problem gambling behaviour.
- Purchase and upgrading of some of the assets of the laboratory facility in Auckland.
- Improving information available to the industry particularly related to industry costs. The Finance function was changed from simply recording and reporting historic data to the provision of information to drive better business decisions (both internally and via, for example, the Transparency Project). An early (priority) focus was to insist on timely financial information.
- Specific investment spends. 'Commitment to industry' initiatives such as the \$10m Fund in the absence of an earlier tax alignment resolution and an increased spend on laboratory, R&D and the Judicial Control Authority (JCA); similarly, NZRB internal investment on, for example, new systems (e.g. FMIS, HRIS).
- To enhance integrity in the industry, the NZRB has been exploring a number of initiatives including changes to where the making of rules relating to integrity issues and the administration/enforcement of those rules are located in the future. A number of steps to enhance the JCA have been identified including a move to a more professional panel and increased remuneration.
- Re-structured Fixed Odds Betting. The NZRB has addressed management, risk and bookmaking issues to vitalize and extend an important growth area of the business.
- Channel improvements such as Self Service Terminals (producing a fundamental shift in customer behaviour), the modernisation of the Bricks and Mortar channel. Also, other initiatives to address customer service issues such as the restructuring of agents' remuneration, the upgrading of selected stores and network planning.
- Establishment of a formal relationship with Massey University (Partnership for Excellence) for industry R&D.
- Revitalisation of on-course events. Declining turnover trends have been reversed, innovations introduced (big screens/Bookies on-course) and new events developed to attract attendance (e.g. Destination Summer Holiday Racing, Christmas at the Races, twilight meetings).
- Internationalisation initiatives – including co-mingling of overseas betting pools. In addition to direct benefits these initiatives have also allowed the NZRB to implement fundamental calendar and funding changes, while opening up the potential for new wagering products (e.g. Quaddies) and the opportunity to develop similar agreements with other territories (South Africa, West Coast USA, Asia).
- Broadcasting reform. Initiatives have included an attitudinal shift for Trackside to become an information and entertainment channel (including magazine programmes such as First Call, Retro) capable of broadcasting 24 x 7, supported by new

investments on new digital outside broadcast facilities and a Te Rapa studio; as well as a full-service radio network.

- Lowered take-out rates for some wagering products.
- Accelerated growth of the sports betting contribution to the NZRB's returns.
- Initiation of changes in relation to education and training in the industry
- Increased funding to New Zealand sporting bodies.
- Successful confrontation of a major biosecurity threat (equine influenza).
- Increased payments to the industry from operating activities including achievement of its original \$100 million target after just three years.

2.3 The Financial Impact of these Changes

This section contains a series of tables prepared by the NZRB specifically for this review. They document the financial impact of the initiatives and changes referred to above.⁹

The first of these tables, shown on the next page, summarises key benchmark indicators to enable an assessment of changes in the principal measures of NZRB performance and, in particular, the growth in the overall surplus on year by year basis. In terms of the latter, they show that the magic \$100m has been achieved. Other tables attempt to identify whether that achievement was primarily a result of advantageous changes in the tax regime or whether the NZRB has a broader basis for defining its achievements.

⁹ The figures for 2008 are forecasts prepared as at the end of May 2008.

Benchmark	2004	2005	2006	2007	2008f
CPI	935	962	1000	1020	1055
CPI % chg	0.0%	2.8%	4.0%	2.0%	3.4%
CPI	0.0%	2.8%	6.9%	9.1%	12.8%
	\$m	\$m	\$m	\$m	\$m
Off course Tote	1,045.8	1,079.6	1,096.7	1,157.9	1,218.6
Oncourse Tote	74.3	74.5	75.3	78.4	81.7
Total Tote	1,120.1	1,154.1	1,172.0	1,236.3	1,300.3
FOB Racing	7.1	18.9	54.4	67.7	80.6
Sports	105.0	100.0	138.3	131.5	140.8
Total Fixed Odds	112.1	118.9	192.7	199.2	221.4
Turnover	1,232.2	1,273.0	1,364.7	1,435.6	1,521.7
Revenue					
Net Betting Revenue (NBR)	171.0	176.8	184.0	227.9	231.8
Export	2.4	3.6	3.8	4.1	12.2
Other Revenue	6.9	8.9	11.1	11.1	11.0
Total Revenue	180.3	189.3	198.9	243.1	255.0
Interest	4.1	5.1	5.8	6.9	7.7
Operating Costs (COGS + Opex + Depr) ¹⁰	107.9	114.1	119.1	128.3	136.5
Abnormals (Asset sales)	1.9	1.6			
Net Surplus (Including Abnormals)	78.4	82.0	85.6	121.7	126.2
Net Surplus (Excluding Abnormals)	76.5	80.4	85.6	121.7	126.2

¹⁰ COGS (cost of goods sold), Opex (operating expenditure), Depr (depreciation)

The following table, 'Normalising Performance', attempts to identify the 'real' growth in NZRB earnings since 2004 after adjusting for increased 'returns to punters' (e.g. reduced take out rates) and the reduction in tax benefit. On this basis the improvement in performance to the credit of the NZRB has been estimated at \$37.4m (48.8%).

Normalising performance	\$m			
	2004	2008 @ 2004 Rates	2008	Variance
TO	1,232.2	1,521.7	1,521.7	0.0
Dividends	993.5	1,226.9	1,249.0	-22.1
	238.7	294.8	272.7	
Duty & GST	60.9	75.2	40.8	34.4
NBR	177.8	219.6	231.9	12.3
Operating Profit	76.5	113.9	126.2	12.3
2008 Forecast				126.2
Back to Punters				22.1
Adjust for returns to punters				148.3
Duty benefit				-34.4
2008 Adjusted Earnings				113.9
2004 Earnings				76.5
Real growth in earnings from 2004				37.4
% Growth				48.8%

The following table estimates the pattern of industry distributions from operating surpluses (based on the same assumptions as above).

Benchmark	2004	2005	2006	2007	2008f
	\$m	\$m	\$m	\$m	\$m
Distributions from operating surplus	77.4	82.05	85.4	112.6	115
Other Distributions	3.968	0.63	2.4	3.2	4
Total Industry distributions	81.368	82.68	87.8	115.8	119

The next table contains a range of performance ratios which measure aspects of operating efficiency and effectiveness.

Benchmark	2004	2005	2006	2007	2008f
Net Betting Margin	13.88%	13.89%	13.49%	15.88%	15.23%
Opex/TO	8.76%	8.96%	8.73%	8.94%	8.97%
Surplus/TO	6.36%	6.44%	6.28%	8.48%	8.29%
Distributions from operating surpluses/TO	6.28%	6.45%	6.26%	7.84%	7.56%
Industry contributions/TO	6.60%	6.49%	6.43%	8.07%	7.82%

The following table illustrates the growth in a range of performance measures.

Benchmark	2004	2005	2006	2007	2008f
Turnover (million)	1,232.2	1,273.0	1,364.7	1,435.6	1,521.7
% change	0.00%	3.31%	7.20%	5.19%	6.00%
% growth	0.00%	3.3%	10.7%	16.5%	23.5%
Operating costs (million)	107.9	114.1	119.1	128.3	136.5
% change	0.0%	5.7%	4.4%	7.8%	6.4%
% growth	0.0%	5.7%	10.4%	18.9%	26.5%
Opex (Operating costs-COGS) (million)	72.3	76.9	79.9	83.4	85.6
% change	0.0%	6.4%	3.9%	4.4%	2.6%
% growth	0.0%	6.4%	10.5%	15.4%	18.4%
Net surplus (million)	79.483	82.056	85.743	121.721	123.217
Returns as a % of Turnover	6.5%	6.5%	6.3%	8.5%	8.1%
Industry Distributions (million)	81.368	82.68	87.8	115.8	119
Cumul. Ind. Dist % chng	0.00%	1.6%	6.2%	31.9%	2.8%
Dist % growth	0.0%	1.6%	7.9%	42.3%	46.2%

2.4 Conclusions

This Part of the report has documented a wide range of initiatives taken by the NZRB since its formation. Undoubtedly, much has been achieved during the period. Other important initiatives have also been identified and commenced by the NZRB (e.g. in relation to industry integrity, infrastructure, supply chain wastage, and customer relationship management) but at this stage these are still ‘works in progress’.

The financial information documented in this section also appears to track a steady improvement in many aspects of the financial well-being of the industry. That good progress has been made in this respect is affirmed by representatives of the various racing Codes who acknowledge that there has been a significant improvement in the financial well-being of their sectors of the industry. On balance, they are positive about the progress that has been made by the NZRB and about future financial projections although they are realistic about the under-investment that has occurred over many years and the backlog of expenditure, e.g. on facilities, which must be caught up.

Not all performance indicators are showing progress, however. High governance/management and transaction costs remain inherent in the way in which the current 3-layer industry structure is operated. Within the NZRB itself, the ratio of operating expenditure to turnover, for example, has remained largely static over the period even

though turnover has increased significantly. On the face of it, operational efficiency gains might have been expected once the initial establishment costs were incurred and as greater economies of scale became available. However, improved services provided by the NZRB to the industry have incurred increased management costs (e.g. 24x7 television programming, Internationalisation), and there have also been increased depreciation charges (e.g. from new OB facilities).

Notwithstanding such explanations, to the degree to which the NZRB remains a 'statutory monopoly' it will continue to be the subject of suspicion that it is bureaucratic, well resourced and overly 'leisurely' in its approach to its affairs. The experience of other organisations that have undergone a transition process like this organisation has begun in the last five years, suggests that further *significant* performance improvement should be expected as culture changes take root and management capability increases.

Code representatives also consider that much remains to be done. To the extent that they are critical of the NZRB their concern is about the slow pace at which some matters largely within the NZRB's control (e.g. the development of new betting products and improved channels) have progressed. For its part the NZRB emphasises it has needed to get the foundations right. There has been a requirement to make a significant investment in systems, for example, before it would be possible to deliver an improved customer experience.

Code representatives also acknowledge, however, that in relation to other aspects of slower progress (e.g. infrastructure and integrity matters), the Code-driven racing industry structure itself is a considerable impediment. The structure incentivises Codes to think of themselves as being in competition with each other for 'market share'. They are protective of their autonomy in areas in which the evolution of better integrated, more efficient and effective industry-wide approaches appear desirable.

Regardless of structural impediments, however, the challenge for both the NZRB, and the industry as a whole, is to 'get better, faster'.

3 Governance Structures and Processes

3.1 Introduction

This Part examines the structures and processes applicable to or adopted by the NZRB to enable it to conduct its affairs in an efficient and effective manner. Its focus is principally on the operation of the governing board of the organisation which has the primary responsibility for the performance of the NZRB.

3.2 Board Composition

The composition of the 7 member governing board is determined by the Act (s.11):

- an independent chairperson appointed by the Minister after consultation with the racing industry;
- 1 person appointed by the Minister on the nomination of New Zealand Thoroughbred Racing (Inc.);
- 1 person appointed by the Minister on the nomination of Harness Racing New Zealand (Inc.);
- 1 person appointed by the Minister on the nomination of the New Zealand Greyhound Racing Association (Inc.); and
- 3 persons appointed by the Minister of Racing on the advice of the nomination advisory panel.¹¹

The provisions of the Act preclude a person who is a chairperson of a racing Code from being appointed to the board. Appointments are made for a period not exceeding three years. The Minister may appoint people to be members of the board only if he/she is satisfied that they are qualified to be members by virtue of their:

- knowledge of, or experience in, the racing industry; or
- expertise in business, marketing, or economics.

In recommending the appointment of three people to the governing body, the nomination advisory panel may only recommend the appointment of any person if:

- the Minister has identified the desired skills and qualifications of nominees and sought the nominations of persons for appointment to the board;

¹¹ Under s.12 of the Act, the nomination advisory panel consists of 5 members:

- the Minister, who chairs the panel;
- the independent chairperson of the Board; and
- the 3 chairpersons of the racing Codes.

- the recognised industry organisations have been given a reasonable period (not less than 4 weeks) during which to make nominations;
- the Minister has distributed a list to the recognised industry organisations of all those persons who have agreed to be nominated to serve on the board;
- the racing codes have consulted their affiliated recognised industry organisations on the list of those persons nominated to serve, and the codes have given those organisations a reasonable opportunity (not less than 7 days), to comment; and
- the nomination advisory panel has met to consider the nominations, taking into account the outcome of the consultation with the recognised industry organisations and the desired skills and qualifications of nominees.

Once nominations are received and advised by the Minister, they are presented to the board which then has an opportunity to consider its own views about the ideal composition of the board and the potential of different nominees to strengthen its membership.

The board Chairman then puts the board's views to the Code Chairs prior to the four Chairs meeting with the Minister. On the face of it, this is both an extended, even convoluted, process, and an inward looking one.

The NZRB's annual reports have, since inception, referred to those of its members who are not Code representatives as 'independent' members of the board. Given, however, that the weight of the consultation process revolves around inputs from industry sources, there is a risk that appointments to the board will be 'industry insiders' or at least those well known and accepted within the industry. While industry knowledge is very important to the board's deliberations, this is presumably the reason for the inclusion of Code representatives on the board. The Minister and others involved in the process should guard against the process (which is, admittedly, largely prescribed by the Act) preventing the possibility of appointments from outside the industry. The appointment process needs to be capable of bringing to the board individuals who will contribute the type of 'intelligent naiveté' that strengthens the capability of any governing board and who will challenge 'conventional wisdom' within the industry. Having said that, it is axiomatic that *all* members of the board should have a sincere interest in the industry.

The current structure of the board includes a representative of each of the Codes. A problem often associated with a representative governance structure is the risk of parochialism and thus of governance underperformance. Whether or not this occurs is very dependent on the calibre and performance of the representatives appointed. Current 'independent' members of the board are very positive about the contributions made by Code representatives and how they provide a window into their respective Codes while at the same time taking an industry-wide perspective. The board considers the Code reps are integral to achieving the right outcomes (e.g. improved collaboration and coordination within the industry). While that view is a tribute to the current 'representative' directors, it is vital that the Codes (which make the appointments) continue to put the best people they can find onto the board and then support them to act in the best interests of the industry as a whole.

While the Act requires the position of chairman to be filled by a person who is 'independent', it is noticeable that the Act does not define what constitutes independence.

Internationally, legislation and regulation in relation to corporate governance is increasingly exact in defining that concept. Arguably, a similar discipline should also apply to other members of the board not defined as ‘representatives’.

Recommendation 1:

That an operational definition of ‘independence’ relevant to the NZRB be developed and applied by the nominations advisory panel in considering future board candidates.

3.3 Board and Board Member Responsibilities

The Act states that all decisions relating to the business or affairs of the NZRB must be made by or under the authority of its governing body in accordance with the most recent statement of intent (SOI) presented to the House of Representatives. The board has all the powers necessary for managing, and for directing or supervising the management of, the business and affairs of the NZRB.¹² The board is empowered under the Act to determine its own procedures.

A board member, when exercising his or her powers or performing duties as a board member, must act:

- in good faith;
- with reasonable care, diligence, and skill; and
- with honesty and integrity.¹³

It is surprising, in the light of the risks that have been identified in other governance environments featuring a board structure that contains elements of ‘representation’, that there is not an additional requirement such that *all* board members must act *in the best interests of the industry as a whole*. While this requirement, which is customary in most governance environments, might be considered implicit, there may be advantage in removing any doubt in future amendments to the Act.

These expectations of board members are consistent with comparable expectations in other legislation and statements of best practice. They are also supplemented by other sections of the Act concerning, for example, the management of conflicts of interest. Sections 8 to 12 of the Act deal specifically with board members’ interests. In addition, in 2006, the board adopted a conflict of interest policy. This took into account not only the provisions of the Act but, for example, relevant provisions in the Crown Entities Act 2004.

The conflicts of interest policy is scheduled to be put to the board for reaffirmation in June 2008 but it appears that the intention is to treat this as a relatively routine matter. As recent inquiries into conflicts of interest in various district health boards have underlined, however,

¹² Section 10.

¹³ Schedule 1, s.1

the handling of conflicts of interest at the governance level is a complex area which demands careful thinking through by any governing board. This is even more important for a body which seeks to influence the behaviour of ancillary industry organisations and which pursues industry integrity as one of its organisation's principal outcomes.

Recommendation 2:

That there is a thorough, 'first principles' review of the current conflict of interest policy.

In both New Zealand and internationally, it is considered best practice for a governing board, particularly of a substantial organisation such as the NZRB, to develop and adopt its own governance 'charter' to 'operationalise' the requirements of any applicable statute and organisation constitution.

Directors are living and working in times when the focus on their duties and responsibilities, and on accountability for their performance, is intensifying. Therefore, the better the functions and operations of the board and its members are defined and understood, the more the scrutiny which they are increasingly undergoing will be satisfied. One step is the adoption by the board of formal board charter, or terms of reference, setting out its and its members' roles and the conduct expected of them.¹⁴

While a limited number of governance-specific policies have been adopted (such as that concerning conflict of interest referred to above), and there are charters for each of the board committees, there is no single document that defines desirable governance processes, consolidates governance policies and protocols and spells out unequivocally expectations for the performance of the board and its members. Such a document would not only provide a starting point for the evaluation of board and director effectiveness but would serve as an effective induction tool for both board members and senior executives supporting the board.

Recommendation 3:

That a board charter or terms of reference be developed to document the board's interpretation of its role and responsibilities and to serve as an accountability framework for the board and individual members.

Another aspect of international governance best practice which is widely adopted in both the commercial and Crown entity sectors in New Zealand is regular board and director evaluation. While the Audit and Finance Committee Charter makes provision for a self-assessment process (and the committee has recently conducted a very comprehensive review of its effectiveness) this practice does not seem to apply to the other committees or, in fact, the board itself.

¹⁴ Institute of Directors (2007). Principles of Best Practice for New Zealand Directors. Page 21.

Any improvement in the performance of boards, and of individual directors, will add value to the company and is accordingly in the interests of the company and its shareholders. It follows that, as part of the following their legal and ethical obligations to the company and its shareholders, directors should be constantly looking to achieve such improvement. One process that should result in improvement, and therefore in adding value to the company, is evaluation. Evaluation in the present context means:

- *The ongoing process of reviewing the performance of the board as a whole, and*
- *The ongoing process of reviewing the performance of the individual directors who comprise the board, including the board chair and committee chairs.¹⁵*

The discipline of a regular, preferably independently facilitated, board and director evaluation process is an important aspect of good governance. If adopted, the board would be demonstrating to the industry as a whole its commitment to increasingly higher standards of board effectiveness and its willingness to hold itself and individual members accountable for their performance. Additional benefits would be to identify professional development needs and opportunities and to inform the process of succession planning as it relates to individual board members.

Recommendation 4:

That the board undertakes a regular self-assessment process covering the effectiveness of the board, the Chair and individual members.

3.4 Other Governance Effectiveness Related Matters

3.4.1 Board Structures

Since the formation of the NZRB its board has made effective use of committees, striking a good balance between the attention that should be paid, collectively, by the board as a whole, to important issues, and the use of board committees to provide input to and oversight of, particular areas of risk or strategic projects. A prime example of the latter was the ‘Taxation Committee’.

Currently there are three formally constituted ‘standing’ board committees:

Dates Committee

Under s.42 of the Act, the board must establish and maintain a committee that, before the end of each racing year, must determine:

- all of the dates in the subsequent racing year on which betting races will occur;
- the allocation of those dates among racing clubs; and
- any conditions of allocation.

¹⁵ Institute of Directors (2007). Principles of Best Practice of New Zealand Directors. Pages 56-57.

The committee must consult with each of the recognised industry organisations on the proposed dates, allocation, and conditions.

Audit and Finance Committee

The Audit and Finance Committee meets quarterly and assists the board in discharging its responsibilities with respect to financial reporting and the financial risk management practices of the NZRB, and the work and performance of both the internal audit function and the board's external auditor, Deloitte.

Unlike the Dates Committee, the Audit and Finance Committee is a true 'governance' committee (i.e. it is established to help the board do its job). It now pays far more attention to a wider risk management framework than when it was originally established to provide the more traditional finance focus. It is common for many boards to have an 'audit and risk' committee and, given the change to a broader role, it may be time to rename the committee the 'Audit and Risk Committee' to better express its real function.

Compensation and Development Committee

Originally called the Remuneration Committee, its purpose is to monitor issues and determine policies and practices relating to the remuneration and review of the Chief Executive and the senior executive committee, as well as overseeing management development and succession planning processes.

Each of these committees support the board by considering relevant issues at a suitably detailed level then reporting back to the board with recommendations except where specific decision-making authority has been delegated by the board. All other matters are dealt with by the board collectively.

Each of the committees has its own written charter, detailing roles and responsibilities, membership, functions, reporting procedures and the manner in which they are to operate. The structure and membership of each committee is reviewed annually. As far as possible the composition of each of the committees reflects board member experience and skill sets.

A review of a selection of committee agendas and papers suggest that these committees are supporting the board in an appropriate manner and are performing effectively and efficiently.

3.4.2 Board Meetings

Over five years the structure of the board's agenda has changed significantly to assist the board in its work. Initially board meetings were dominated by financial and performance reporting and, understandably, matters related to the establishment of the organisation. The early placement on the agenda of the Chief Executive's report and other operational reporting reinforced the operational focus.

The agenda for board meetings today is driven by a range of stimuli. For example:

- previous outstanding issues/agenda items;
- requests at previous board meetings for management to provide an update/overview of an issue discussed/raised;
- issues/approvals that require board input according to delegated authorities;
- items that management believe the board should have an awareness of;
- feedback from board committee meetings;
- other standard agenda items (e.g. financial accounts, media releases, etc).

Board meetings during 2008 appear to have spent less time on the traditional preliminaries which are potentially time wasting and distracting.¹⁶ While the Chief Executive's report is still high on the agenda, preceding this is an earlier part of the meeting labelled 'Strategic'. This sequencing is potentially of great value. However, it is a moot point whether it is yet achieving this potential as the definition of what is 'strategic' is essentially a distinction between 'business as usual' activities and those initiatives/activities/actions that are 'one off', emerging, investment focused or have an impact on the current business model.

In formulating the agenda, the normal practice is for the Chief Executive to work with senior management to identify items for the forthcoming board agenda. While this is also discussed with the Chairman, what goes onto the agenda appears to be primarily a management 'judgement call'.

Regardless of the type of organisation, board agendas driven by management in this way inevitably have a strong operational focus and it appears that such is the case in relation to the NZRB. The type of management reporting that supports such an agenda compounds the tendency to draw a board's attention down into the organisational entrails. As a consequence, a board's primary focus is not future facing and strategic, but rather backward looking and operational. This is often a consequence of a board's failure to determine and then focus on its own job rather than of deliberate management intent. In an industry like racing that has a tradition of being very 'political', it could be expected, however, that boards at both industry and Code level would be susceptible to pressures for micro-management. NZRB members commented that, to-date, micro issues have often driven the macro ones but, nevertheless, this is something both board and management alike will need to work hard to resist.

Later in this report attention is drawn to the need for the NZRB to provide more effective strategic leadership to the industry. The starting point for this is to change the way the board spends its own meeting time to ensure that it has adequate time to concentrate on higher level industry issues and to review whether operational management is succeeding in delivering desired outcomes.

An effective way of doing this is the determination of a board work plan or 'annual agenda' which has primarily a governance level focus. This longer term view of how and where the board must add value then drives specific meeting agendas. An annual agenda usually has two main components. The 'baseload' of the board's work that concerns a variety of *non-*

¹⁶ For example, confirmation of the minutes of the previous meeting is the *last* item on the agenda.

discretionary items – e.g. the fulfillment of compliance obligations, performance monitoring, etc - which will usually be advised by management. These should be scheduled throughout the year to ensure that they do not dominate any one board meeting. More importantly, from the board's perspective, however, are the *discretionary* items – the key strategic and policy issues requiring concentrated and possibly extended attention by the board. Typically non-discretionary items carry a sense of urgency which discretionary topics do not. An annual agenda setting process would assist the board and management to differentiate between matters which, at the board level, are 'important' as opposed to merely 'urgent' and which otherwise get crowded out by apparently more pressing matters.

The board should give itself the opportunity through an appropriate planning session to develop a collective consciousness, with input from senior management, about these discretionary topics and the board's interest in them. This would be aided by being able to refer to the type of higher level strategic intent document referred to later in this report. These 'discretionary' topics should then be built into the future board meeting schedule. Successive board meetings would then be structured so that these strategic and policy issues that the future of the industry occupy both the early part of the agenda and the greater part of the board meeting running time.

While the structure of board meetings has been evolving in a useful direction, further changes may be advantageous. For example, currently 'matters for decision' most commonly appear under the heading of the relevant work stream (e.g. racing and wagering, broadcasting, distribution, etc). A structure which has been proven to work extremely well for many boards features the following broad sequence:

- **Preliminaries** – e.g. confirmation of the agenda, declarations of conflict of interest etc
- **Matters for *discussion*** – e.g. changes in the operating environment, strategic issues drawn from the annual agenda, scoping papers in relation to matters requiring future decision, etc
- **Matters for *decision*** – on matters that exceed management delegations.
- **Matters for *information*** – performance monitoring reports etc.

Further evolution along these lines would not only improve the 'flow' of board meetings but create a structure around the board's roles and responsibilities that would help overcome the tendency for operational work streams to dominate the board's attention. The risks to the board's effectiveness of an undue focus on operational matters are a matter which is explored further in later sections of this report.

Recommendation 5:

That the board develops and implements an annual agenda setting process to give greater focus to key strategic issues.

Recommendation 6:

That the board makes further changes in the structure of the board meeting agenda to improve the flow of board meetings and encourage a governance rather than operational focus.

3.4.3 Board Papers

Any board is highly dependent on the timeliness and quality of papers prepared for board meetings by management.

The 2008 board meeting schedule provides for board papers to be distributed on the previous Wednesday providing members 3 clear working days before the next board meeting on Tuesday the following week. The board paper 'pack' for meetings is generally manageable (less than 100 pages) so this is probably sufficient time for preparation although many boards require papers at least 5 working days ahead of a board meeting.

By themselves board papers reviewed were generally informative and their logic easy to follow. Taken overall, however, certain aspects could be further developed to the benefit of both board and management alike.

- Board papers generally would benefit from an improved and consistent structure. The existing template for board papers relates primarily to formatting (font size etc). It would be worthwhile developing a standard template for the *structure* of board papers that would assist both the board members in reviewing papers and staff in preparing them.
- While some papers are well structured, others launch into the substance of the paper without the type of introduction that provides a connection to past board deliberations and a context (e.g. reference to relevant policy or business plan objective).
- Not only longer papers would benefit from an overview or executive summary that captured the gist of the paper on the first page. It is often necessary to go right to the end of a paper to get the sense of what the paper is addressing and where it is going.
- Board agendas and papers are replete with acronyms - often (but not always) defined in the body of the papers. It would be of assistance if a regular insert to board papers was a cumulative 'key terms and definitions' sheet(s).
- Board papers prepared to support specific agenda items generally state clearly whether it is a matter for information or a matter for decision. Papers requiring a board decision generally lead with recommendations at the head of the paper. However, there is a tendency for the articulation of some recommendations to be longwinded, containing the rationale as well as the recommendation itself.
- Recommendations are not always numbered.

Notwithstanding these comments, for any given purpose it is up to the board to decide for itself what information it needs and the form in which that information should be presented. Therefore, the board should periodically conduct its own 'audit' of board papers. Pragmatically, it is often useful to link such a review to the arrival of new board members when it is possible to benefit from their 'fresh eyes' and to ensure that their expectations are taken into account.

Recommendation 7:

That the board review the present pattern of board papers with the intention of having these recast to better align with the needs of the board for governance-related information (see also Recommendation 13).

Further comments on opportunities to improve the functionality of board papers are contained in Part 6 of this report.

3.4.4 Governance Statements

Each annual report produced by the NZRB, since its inception, has contained a governance statement consistent with those required to be published by publicly listed companies. The content of those statements has described:

- the board's role and responsibilities
- the board structure and composition
- board processes
- board committees

While brief and limited in scope compared with the best listed company and not-for-profit organisations¹⁷ it is commendable that the NZRB has voluntarily included such a governance statement in each of its annual reports. Consistent with the importance NZRB places on the production of the report, these statements could, however, be expanded to enable stakeholders to gain a more informed view of the challenges facing the board and how it is governing the NZRB. One of the matters that appears to be of interest, for example, outside the organisation, is how the board manages the governance performance risks inherent in the board's 'representative' structure.

The scope and content of the statement should be suggestive of a governing board that is dedicated to attaining 'best practice' corporate governance standards. This would be appropriate given the NZRB's focus on integrity in the industry and the need for it to provide leadership (e.g. through being an effective role model) to the racing Codes and the wider industry.

¹⁷ As compared with companies and organisations receiving recognition through the judging of annual reports by the NZ Institute of Chartered Accountants.

Ideally, in keeping with best practice, the governance statement itself and aspects of the board's governance processes and practices referred to the statement (e.g. board and committee charters) would be available for perusal on the NZRB website.

Recommendation 8:

That the governance statement in the annual report is expanded to provide more information on governance challenges, structures and processes and that it and related material be accessible via the web-site.

3.4.5 Board Member Induction

To ensure that a new board member becomes an active contributing director as soon as possible, induction is a vitally important process that is neglected in many organisations. The most recent addition to the board was taken through a process involving a full day of management briefings and a thorough walk through of the challenges facing the business and the industry. Equally important, however, is the way in which a new board member is introduced to the dynamics and perspectives of the board. This is a responsibility primarily of the board chair.

3.4.6 Chief Executive/Senior Executive Performance Management

A board only has one point of direct leverage over the organisation's performance because it has only one employee: its chief executive.

The NZRB board manages its employment relationship with the Chief Executive primarily through its Compensation and Development Committee. There is an annual performance plan which also covers each of the Chief Executive's direct reports. The key drivers of this plan are established by the committee usually around September each year. There is agreement on key result areas (KRAs) covering financial targets, business priorities, and people leadership and development objectives. Each of these is weighted differently for the Chief Executive and for each of his direct reports according to the nature of their respective roles.

This plan is used as the basis of an ongoing performance review process throughout the year and for the determination of 'at risk' remuneration payments at the end of each season. At intervals, the committee discusses the year-to-date performance of each member of the Senior Executive Committee (SEC).

In concept, this seems likely to be a systematic and effective approach.

3.5 Conclusions

As later sections of this report describe, the NZRB has pursued a systematic approach to setting and fulfilling its objectives. Both the performance and efficiency of the organisation have improved steadily and materially over the five-year period since its establishment. This, of itself, would suggest that has been, at least, adequate governance in the organisation and this report does not suggest otherwise. However, as this part of the report has shown, there are opportunities to develop a more robust 'governance infrastructure' more typical of the best governed organisations and to which an organisation like the NZRB should aspire given the nature of its business, the risks within its industry, and the nature of its stakeholders. Given its industry leadership role and the need for improved governance performance in the wider industry the NZRB should be aiming to demonstrate the highest possible standards of governance and expecting other entities in the industry to follow.

4 The Establishment of Objectives for the Performance of NZRB Functions

4.1 Introduction

This part addresses the process by which the NZRB has established objectives for the performance of its functions (in essence, how the Board has gone about the articulation of its purpose and functions and the determination of its priorities).

4.2 Creating an Evidential Basis for Objective Setting and Strategic Planning

When the NZRB was established it faced a variety of significant challenges to the performance of both the new organisation and the industry as a whole. For example:

- creating and staffing a new organisation;
- forming effective working relationships with key stakeholders – especially the Codes;
- industry fragmentation and parochialism – overcoming the widespread ‘them and us’ attitude;
- declining industry performance (e.g. market share lost to casinos and poker machines; reducing foal crops; pressure on stakes, etc); and
- the need to lift professionalism throughout the industry.

These and other related challenges were, in the main, very familiar to industry leaders. When first formed, however, the NZRB found that much of the available racing industry information was either anecdotal, or not in a usable form.¹⁸ An essential starting point for setting objectives and establishing priorities was, therefore, the development of an evidential basis. The following are examples of the approach the NZRB has adopted to overcome this problem.

4.2.1 The IER Economic Impact Study

To develop a future plan for the industry, the NZRB needed hard economic data. In its first year of operation the NZRB engaged IER (Australia) to study the size/scope of the industry and for customer research purposes. This major economic study on the New Zealand racing industry provided an important fact base, overcoming historic reliance on anecdotal evidence. Some of its key findings were referred to in Section 1.4. It provided not only the NZRB but stakeholders (including the Government) a real measure of the economic

¹⁸ Chairman's Report. New Zealand Racing Board Annual Report 2004

importance of the industry. It also was a significant driver for the organisation's business planning for the first two or three years of its existence.

4.2.2 The BCG Performance and Efficiency Review

In addition, to the fact-based economic research, the Board also commissioned a performance and efficiency review of the NZRB. This was undertaken by the Boston Consulting Group ('BCG').¹⁹ The primary objectives of the BCG review were:

- to understand the underlying drivers of performance; and
- to establish a fact base from which to drive management decision-making.

The review also identified and quantified, in a preliminary way, a number of potential performance improvement opportunities.

The picture painted by the BCG review of recent and current industry performance was not a positive one because:

- TAB performance had been largely static over the previous 5 years (e.g. turnover growth 1.7%; operating surplus growth 1.2%; only 'middle of the pack' in terms of operating cost efficiency).
- Domestic racing was in decline in all 3 codes (thoroughbred, fewer races and fewer bets per race; harness and greyhounds, fewer bets per race).
- Increasing volume of overseas product, but diminishing contribution (lower turnover per race and higher costs).

In comparison, however, sports betting was enjoying strong growth, albeit from a low base.

The BCG research suggested there were significant potential gains for the industry that were likely to come from:

- increasing participation;
- growing revenues;
- reducing costs/efficiency; and
- increasing industry performance and efficiency.

The review concluded that there were several substantive and interlinked industry issues that needed to be tackled to make these gains possible. These were the need:

- to increase participation of owners (and hence increase horse numbers);
- for a more managed racing calendar; and
- to align club payment formulae with individual club and overall industry objectives.

¹⁹ Boston Consulting Group. Review of Performance and Efficiency. 29 June 2004

Along with the IER study, undertaking this second major study in its first year helped the NZRB to identify a range of challenges and opportunities including the need for:

- Performance improvement, particularly in the distribution system of the NZRB focusing on changes to the betting channels and outlets. This led the Board to state that it “...will be aggressively pursuing opportunities to improve performance, identified at \$10-15m by the review.”²⁰
- Increased participation in domestic New Zealand racing and improved TAB performance.
- Industry wide understanding that racing is entertainment and the significance of this in a marketing sense. *“The industry cannot prosper simply by doing more of the same. The industry desperately needs more participants, new customers, better economic outcomes for owners and more people attracted to racing simply to have fun.”*²¹
- Change in, for example, racing calendar and funding arrangements in order to deliver the best possible improvement platform.

The first year’s results underlined concerns about:

- a continued decline in domestic betting turnover; and
- an even steeper decline in on-course participation.²²

As a result of obtaining a better understanding of the industry and its place in the economy, the NZRB adopted three major performance improvement objectives:

- to improve the NZRB’s performance on behalf of the industry;
- to revitalise the racing industry;
- to establish the right platform for the racing calendar and funding in order to get the full benefits of the other improvements.²³

4.2.3 The Taxation Task Force

Another major concern to the industry and the NZRB in its formative years was the issue of taxation. A higher level of taxation was placed on race wagering in New Zealand compared to the taxation of other forms of gambling. The NZRB was conscious of the need to secure sufficient funding to meet its obligations under the Act, which includes promoting the economic development of the racing industry. It had also been conscious of criticism within the industry for “not doing enough” to force a favourable outcome on the taxation issue. Rectifying the tax anomaly was considered a fundamental element of any major industry plan to improve the international competitiveness and performance of the New Zealand Racing Industry. The board’s position, however, was that success in such an endeavour was

²⁰ Chairman’s Report. New Zealand Racing Board Annual Report 2004

²¹ *ibid*

²² Chief Executive’s Report. New Zealand Racing Board Annual Report 2004, p.7

²³ *ibid*. p.10.

ultimately dependent on convincing officials of the quality and logic of the argument for equalisation, ahead of any political consideration that might be exercised by Ministers.²⁴

In 2005, to address this issue, the board established a board task group which completed and submitted to the Government a comprehensive report on the taxation of race wagering in New Zealand which proved the case for tax and duty re-alignments. The NZRB had hoped that at least a staged change to rectifying the identified taxation inequity would begin with the inclusion of taxation adjustments to racing in the 2005/06 Budget but officials requested additional information to develop the Government's response to the case submitted. This work was the basis for the Racing Minister's tax package which was introduced in the 2006/07 year. Its major beneficial impact is apparent in the analysis contained in Section 2.3.

4.2.4 Industry Transparency Project

The Industry Transparency Project was established in August 2005 to better understand the revenue and cost structures of the NZRB. The project took a multidimensional view of the organisation demonstrating contribution by code, selling channel and wagering product. The four integrated models resulting from the exercise produce turnover estimates based on the domestic calendar versus imported product opportunities and outline the key cost drivers of the NZRB. It recognised that the NZRB incurs costs and utilises assets in two main activities:

- Wagering (Selling, Network, Sport (Fixed Odds), Marketing, Television and Radio Transmission and Programming and IT Support).
- Venue services (On-Course services, Jetbet, Judicial Video and Outside Broadcasting).

The intention was to initiate a process where all affected parties might collectively agree to pursue opportunities to improve industry returns. Through analyses of the calendar and the cost and revenue drivers, the project was designed to assign costs enabling a determination of the extent to which each product contributed to the overall NZRB performance.

4.3 Strategic and Business Planning Processes

The most important process in any organisation for establishing objectives begins with its strategic planning process. The way the Act is written and the way key industry stakeholders think about the NZRB's role, underlines the expectation that the NZRB has a vital strategic leadership function that extends well beyond the organisation itself to the wider racing industry. However, the structure of the industry means that the NZRB has limited, if any, direct control over many important aspects of implementation of any industry wide planning it may aspire to undertake. This is particularly true where it relies on the racing Codes for effective implementation of aspects of its wider responsibilities as, for example, in relation to important aspects of 'integrity'. The NZRB is, therefore, dependent to a significant degree

²⁴ Chairman's Report. New Zealand Racing Board Annual Report 2005. p.4

on its ability to exercise *influence*. It's strategic and business planning processes are, potentially, critical tools for gaining and exercising influence. The way it goes about these processes is, therefore, central to its effectiveness.

4.3.1 Business planning

Business Planning Process and Timetable

Under the Act (s.20) the NZRB must, before the commencement of each racing year, prepare a business plan. It is also a requirement of the Act that the NZRB must consult with each racing Code in respect of this business plan.

The process of developing a new iteration of the business plan each year starts, in effect, around September/October the previous calendar year, when engagement starts over the shape of next year's racing calendar. Decisions here feed into the NZRB funding model. At the same time senior management start looking at various challenges facing the organisation and the industry, taking into account performance to date. In recent times, a detailed environmental analysis has been presented to the board in November.

Typically, the next step is for a 'first pass' of the business plan to be presented to the board in February. The objectives of that presentation are as follows:²⁵

- to confirm board support of the Base Plan
- to outline the financial assumptions of the Base Plan
- to outline the balance sheet impact of the Base Plan
- to outline industry impact/requirements
- to discuss the board's appetite for particular opportunities
- to outline the next steps

Following this, the draft plan goes to the Codes for consultation as required under the Act and then back to the board for approval and sign-off in March. The final business plan is then distributed to the Codes. This facilitates the finalisation of Code business plans within the framework set by the NZRB business plan. Because of the interdependence of the 'commercial'/wagering and the industry 'production' sides of the business (including clubs and a number of the other industry organisations involved), alignment between these different levels of planning is critical.

Ideally (and practically), Code business planning would have started much earlier and it is a moot point whether it is desirable for any organisation to finalise its business plan so far in advance (at least 4 months for the NZRB) of the start of a new financial year.²⁶

However, the Codes report general satisfaction with the nature of the engagement between the NZRB's business planning process and their own. While acknowledging that the NZRB's approach to business planning is essentially a 'top-down' process, Codes have a

²⁵ Based on the February 2007 presentation.

²⁶ Note, however, that the Draft Budget is dealt with separately from the Business Plan and is not presented to the board until May when it approves Code Business Plans, and not finalised until June.

sense of inevitability about this given the cascading nature of key decisions in the industry. The significant degree of direction by the NZRB of Code business plans (e.g. pressing Codes to indicate how they will implement aspects of the NZRB business plan) is also accepted.

While there is a potential timing issue if, as this year, there are outstanding issues with the NZRB business plan, Codes have not experienced the NZRB plan changing dramatically from one year to the next, and with reasonable certainty now around base funding, there is a degree of predictability that enables Codes to get on and produce their own business plans more or less in parallel.²⁷

The Codes acknowledge that clubs face a similar challenge in producing their business plans which depend on Code level decisions.²⁸

The NZRB process described above suggests that the strategic direction of the organisation is primarily management-driven. The established (and accepted pattern) seems to be for the board to engage in strategic direction setting primarily by responding to management business planning initiatives. If this is the case, no matter how effective the board is in scrutinizing and critiquing management proposals, it is always going to be in a reactive position.

Different governing boards have varying philosophies about the degree to which they should engage proactively in the development of corporate strategic direction. Emerging international best practice suggests that the most effective boards do not want to be primarily limited to monitoring management. Engaging actively with management at the 'front-end' of the strategic and business planning process allows a board to agree high strategic and policy directions that provide a strategic framework for the application of management expertise and detailed knowledge of the business to more detailed planning. In contrast, responding to concrete management initiatives as they appear draws a board into 'second guessing' (potentially frustrating) management and encourages piecemeal rather than holistic, systemic thinking. The Codes and industry organisations appear to be placed in the same position; reacting to NZRB management initiatives.

The November board discussion on the operating environment would be an ideal opportunity for the board to engage in the type of dialogue with the management team that would give it a more proactive role in the framing of strategic objectives and priorities. This would also be of assistance to management in the subsequent preparation of a business plan to achieve those board-set/agreed objectives and fulfil its priorities. There is also a place for far greater board concentration on the development of the Statement of Intent (SOI). Further comment is made on this below.

²⁷ One estimate is that as much as 80% of a Code business plan can be completed in advance of receipt of the draft NZRB plan.

²⁸ There are other industry organisations which also have a high level of dependency on NZRB funding decisions but, by contrast, these are funded on a year by year basis (e.g. the Equine Industry Training Organisation) and have comparatively little certainty from one year to the next.

Business Plan Content²⁹

The NZRB does not prepare a ‘strategic plan’ as such. To the extent that it is apparent, the NZRB’s strategic intent is expressed in the context of a business plan that typically covers a three year time horizon. Given the major and long-term challenges facing the industry it is somewhat surprising that a longer term view has not been developed and published, at least within the industry. Industry statistics published by the NZRB typically look back over at least the last 10 years and these indicate how important a longer time frame is to change in the industry.

Many of the challenges facing the industry deal with matters that cannot be resolved within a three-year time horizon. The development of the necessary industry capacity and capability is, inevitably, a long term ‘project’. New entrants who wish to develop careers in the industry (e.g. as breeders, trainers, jockeys, etc) should reasonably expect the industry’s peak body to articulate a longer term view of the industry. Clubs, for example, considering significant infrastructure investments will have to take a long-term view of the economic viability of those investments. Many of the social and demographic trends affecting the industry (e.g. attitudes to gambling; the aging of industry stalwarts, etc) are also longer term.

Successive business plans produced by the NZRB since 2005 have adopted a similar but evolving format. The most recent of these (2009-2011) is the most comprehensive and detailed. It is apparent that the business plan format has been significantly influenced by the statutory requirement to consult with the three racing Codes. The plans are expressed primarily in the form of narrative descriptions and explanations. In that sense each plan appears to have been written primarily as an information memorandum – to explain (e.g. industry trends) and inform (e.g. about the NZRB’s future intentions). Typical content has included:

- an introduction/overview (of the plan)
- a summary table of achievements against the previous season’s planned initiatives
- an analysis of industry trends and challenges
- an outline of planned initiatives – predominantly in the form of intended actions and activities
- funding – e.g. indicative base funding allocations to Codes
- requirements for Code business plan content³⁰

In the initial 2005-2007 business plan there was a statement of vision (“*Grow the Racing Industry Sector by being a dynamic global leader in the responsible gambling and entertainment business*”) and values (“*Exceed expectations through teamwork, integrity and passion.*”) but such high-level statements have been conspicuously absent in later versions. The further development of corporate values, for example, appears to have become a ‘bottom-up’ process without Chief Executive and/or SEC direction.³¹ While there are benefits in such an approach (e.g. staff ‘ownership’ and commitment to the values thus articulated) there are also risks to the

²⁹ Note that the following comments relate to a critique of business plan presentation and content not to the actual achievements made by the NZRB to date.

³⁰ The absence of an index of contents in any of the plans makes comparison difficult.

³¹ Vision and Values. New Board Member Induction presentation, August 2007

organisation in not having a firm direction from board and senior management on what is, essentially, the basis for setting behavioural expectations.

With the exception of that first plan the content of subsequent plans has been primarily operational in tone and content. This is consistent with comments above concerning the apparently management-driven nature of the plans. It should not be taken as a criticism except in the absence of a higher-level, longer term and outcome oriented, strategic plan.

While strategic themes are identified in some plans, the 'planning' content of the plans is typically expressed in the form of planned actions or *activities* (e.g. "*Channel Transformation (Project Everest). The transformation of channels will be addressed through a coordinated project. This project seeks to lay a platform on which to optimise the Brand and will...*"³²).

With the possible exception of references to the \$100 million target in earlier plans there are almost no *outcomes* specified. NZRB business plans are about 'what we are going to *do*' not about 'what we are going to *achieve*'. This is reinforced by the construction of most of the business plans around specific work streams.

Now that the \$100m target has been achieved there is no sign in the most recent business plans that an equivalent new target has been set. Indeed, there were surprisingly few numbers included in the earlier plans and then seldom as unequivocal performance targets (e.g. "*These and other initiatives within the NZRB are tasked to identify \$10-\$15m of operating efficiencies over the next three years.*"³³). Early business plans were full of 'might' and 'may' type statements. They featured (and still do) financial forecasts rather than financial *plans*. The 2009-2011 business plan is still forecast-oriented but includes, for example, three-year financial projections for a number of operational activities along with a variety of performance ratios that provide a basis for monitoring changes in efficiency over time. To some degree, therefore, the most recent business plan may be an exception to the previous pattern and may mark the start of a new trend.

As a consequence of the continuing absence of outcome targets, reporting of achievements against a previous year's plan is largely confined to 'updates' on projects and other initiatives (e.g. "*Consultation phase commenced with clubs and consortiums as stage one of oncourse service delivery.*" "*Synthetic Tracks project in progress.*").

The failure to state (and then report against) outcome-oriented performance targets with real 'stretch' attached to them makes the NZRB open to criticism, particularly given its stated value of 'exceeding expectations', that it is setting for itself soft 'targets' against which it is comparatively easy to report progress - of a sort. As a consequence, it would be very hard for external stakeholders to hold the NZRB, or the board hold management, accountable for its performance in terms of achieving tangible outcomes. Perhaps not surprisingly, therefore, Code representatives expressed frustration about the time it has taken the NZRB to implement key strategic decisions (e.g. co-mingling, synthetic tracks, rationalisation of facilities, etc). At the same time it must be acknowledged that, under the current

³² New Zealand Racing Board. Business Plan 2009-2011, p.61 (note: page reference refers to sequence in the relevant board agenda)

³³ New Zealand Racing Board. Business Plan 2007-2009, p.14.

arrangements, the NZRB cannot dictate to the Codes which, historically, have wanted to retain control over some of these matters.

While the business plans reviewed appear likely to succeed as *information* documents it is difficult to see them being successful as *consultation* documents because they do not crystallise critical industry issues and invite the Codes to comment on and engage in a dialogue about those and vital NZRB business objectives (including key performance targets). These documents principally draw the reader's attention to a welter of specific planned management initiatives with which, for the most part, it would be difficult to disagree even if they were particularly germane to the Codes' interests. Comments from Code representatives reinforced the conclusion that while there is generally an active engagement between the Codes and the NZRB, the process of consulting on the NZRB's draft business plan, as such, is not central to this engagement.

This could be, in part, because the 'weight' of the content of the NZRB's business plans over the five-year period has been on the income generation or 'commercial' side of the business. The Codes are happy to concede that the NZRB is the source of expertise on this dimension of the industry and do not presume to second-guess the NZRB on that score.

A concern amongst the Codes, which is not difficult to predict from this analysis, is that the NZRB has failed to articulate a longer-term vision (or 'headline strategy') of where the industry should be in five to 10 years time. There is a clear sense that this is part of the NZRB's job. There is a view among some Code representatives that it should take a tough-minded approach to shaping the future of the industry including addressing the need for further restructuring (e.g. away from a code focused model) and other changes to the Racing Act. As one Code representative explained it, "*the NZRB seems to be too busy dealing with day-to-day issues to step back and take a longer term view. It seems to think that as long as revenue is OK it is all right for it to just trundle along*".

Function	Priorities	Activities
Income generation	Wagering	<ul style="list-style-type: none"> • Use Internationalisation strategy to drive wagering and export growth • Market FOB to wider audience
	Distribution	<ul style="list-style-type: none"> • Lift TAB brand perception and service standards • Develop Channel strategies to drive new participation and deliver better standards to current customers
Governance and funding	Integrity	<ul style="list-style-type: none"> • Establish an integrity framework with monitoring and enforcement that will encourage a positive perception of the industry
	Infrastructure	<ul style="list-style-type: none"> • Sponsor an infrastructure investment programme to deliver a sustainable, robust domestic industry • Implement a transparent, consistent funding framework to continue to drive improved returns to participants and support a sustainable domestic industry

Appearing in both the 2008-2010 business plan and SOI was this table summarising the key 'pillars' of the NZRB business plan. Interestingly, during the most recent induction of a new board member this was described as 'the strategic plan'.

While the table is a useful tool to understand how the NZRB thinks about its general approach, it does not explicitly constitute a strategic vision. It is more a summary of what strategies it is going to deploy and how it will organise its work streams. Given the essentially operational focus of a business plan, a more obvious place to look for some expression of the NZRB's higher level strategic leadership intentions might be the statement of intent (SOI).

Recommendation 9:

That the NZRB consider revamping its business plan to better articulate planned outcomes (including project milestones and financial targets) and priorities and to facilitate more meaningful consultation with the Codes about both planned outcomes and strategies to achieve those outcomes.

4.3.2 Statement of Intent

The NZRB is also required under the Act (s.19) to produce an SOI. To be delivered to the Minister before the commencement of each racing year, the SOI relates to that year and each of the two subsequent years.

The SOI must set out, for each racing year to which it relates:

- the objectives of the Board;
- the nature and scope of the activities to be undertaken;
- the performance targets and other measures by which its performance may be judged in relation to its objectives; and
- a statement of accounting policies.

Before delivering the SOI to the Minister, the Board is required to consult the 'recognised industry organisations' on the proposed statement. The Minister must present the SOI to the House of Representatives.

In strategic planning terms both the requirement to present the SOI to the Minister and table it in Parliament, and the sequence of the applicable sections in the Act (the SOI provision is listed before the business planning requirement), suggest the SOI should be accorded an appropriate degree of primacy. It should express the NZRB's strategic intent and best thinking about the future direction of the organisation and the industry. It should provide an 'umbrella' strategic framework from which more detailed business planning at both NZRB and Code level could proceed.

The NZRB acknowledges treating the preparation of the SOI as primarily a compliance exercise. The cover pages of successive SOIs have acknowledged this by stating that *“The Statement sets out the information required under Section 19 of the Racing Act 2003...”* Although it is a public document it is not accessible via the NZRB web-site suggesting it has little status within the organisation.

Practice within the NZRB is for the SOI to be produced towards the end of the business planning process (typically the SOI is approved by the board for progressing to the consultation phase in May). As a consequence of this timing, notwithstanding the requirement to consult with the ‘recognised industry organisations’ (i.e. to go beyond the Codes) the prospect of real *consultation*³⁴ is severely limited. Not surprisingly, advice received from within the NZRB and from other industry sources suggests that there is little industry engagement with the SOI process. For their part, it would seem that industry organisations do not appreciate the potential the SOI process offers to engage directly with the board of the NZRB on matters of strategic significance for them and/or the industry as a whole.

NZRB SOIs produced to date have been minimalist documents prepared primarily to comply with the publication of information required by the Act. For example, the SOI covering the financial years ending 31 July 2008 to 31 July 2010 includes:

- a statement of the relevant aspects of the Act (statutory objectives and the nature and scope of activities of the NZRB);
- a tabulated summary of performance targets and other measures by which the board’s performance may be judged in relation to its objectives
- an indication of a range of activities that will be undertaken in pursuit of priorities and broad timelines; and
- a statement of accounting policies.

Interestingly, this is far more information than was provided in earlier SOIs and may indicate a new approach by the NZRB. Even this more extensive document remains quite different, however, in both content and, apparently, application from the more substantive type of SOI that is produced by most Crown entities. Increasingly, the practice within the Crown entity sector is for the SOI to replace a separate strategic plan.

In terms of its statutory purpose, an SOI is a basis for consultation with key stakeholders about their expectations of the NZRB. By stating ‘upfront’ what the organisation is aiming to achieve, it should be the ultimate accountability document against which the NZRB reports publicly.³⁵ As an accountability document, however, it is somewhat ‘soft’ and could be improved in a number of respects notwithstanding that the minimalist, compliance approach adopted has apparently been acceptable to key stakeholders.

³⁴ Case law on consultation in New Zealand has established that the body consulting must be open to being influenced by the consultation process.

³⁵ The auditor was advised by the Chief Executive that the organisation’s investment in communicating with stakeholders is primarily vested in the preparation of an informative annual report. However, regardless of its purpose and its quality an annual report is prepared ‘after the fact’.

The principal shortcoming of the document itself is that, like the NZRB business plan, it is essentially ‘activity’ oriented. It lists functions and the activities planned in relation to those functions. It is thus another description of what the NZRB is going to *do* rather than what it is going to *achieve*. Even more so than for the business plan it would be preferable for it to be expressed in ‘outcome’ terms. For example, a particular (and surprising) deficiency of the SOIs reviewed, given that one of the two primary functions of the organisation is ‘income generation’, was the absence of financial targets.

These deficiencies in the SOI are particularly relevant to the concern about the NZRB’s perceived failure to articulate a strategic vision for the industry and to engage industry players in an ongoing dialogue about that vision. In one sense criticism of this nature is unfair as it is apparent that on many occasions since the NZRB’s formation its representatives have spoken to the industry about the challenges it faces and the initiatives the NZRB has planned. Some Code representatives say they have a reasonably good sense of what the NZRB is trying to achieve. If anything it is lacking, therefore, it is a succinct document articulating the NZRB’s view of the future and the key results it plans to achieve.

It would not seem particularly difficult, if the NZRB was to reframe its approach to the preparation of the SOI, to use the process required under the Act as a catalyst for the type of dialogue that could lead to and crystallise the thinking required to produce such a document. For example, by bringing industry leaders together, at least annually, before the business planning process begins, with the express purpose of engaging in discussions about both the longer term future of the industry and shorter term priorities, all parties would be better placed to fulfil their own particular responsibilities. There is nothing inherent in the Act to prevent this process occurring in, say, August/September to reflect on the season just completed and to contemplate the future before detailed business planning gets underway.

The Code-driven industry model adopted by the 2003 Racing Act is inherently fragmented and contains a significant degree of inbuilt tension between the relatively autonomous but interdependent component parts. These weaknesses appear to be increasingly well recognised and may, in time, lead to greater integration and other changes some believe would produce further significant improvements in both the efficiency and effectiveness of the industry. In the meantime, however, a collaborative strategic thinking process is needed both to mitigate the weaknesses in the present model and to provide the leadership needed to take the development of the industry to the next stage.

Long-time participants at NZRB and Code board level speak of significant improvements in the relationships between the national body and the Codes over the past 5 years. This reflects a number of factors such as improved reporting and the more frequent opportunities NZRB and Code representatives have to meet. One of these opportunities is the post (NZRB) board CRIG³⁶ meeting. However, while Code participants say that the CRIG meetings are useful they do not provide an opportunity for the type of strategic dialogue that is needed. Participants are not always present in person, often joining via teleconference.

NZRB representatives also lament that the CRIG meetings do not facilitate the type of feedback from Codes that would be useful. Another, related, concern of the

³⁶ Combined Racing Industry Group

NZRB is its perception that the consultation process is largely one-way – that the NZRB is expected to consult with Codes but the Codes do not reciprocate this. Such concerns are typical of governance structures like that which exists in the racing industry. For the industry to function effectively and efficiently it requires a high degree of proactivity in communication and relationship management among all the key parties in order to resolve the inevitable boundary conflicts³⁷ and to build the level of trust and mutual confidence which is necessary given their fundamental interdependence. Regular, face-to-face meetings are essential to develop this relationship and to give effect to the highly effective collective leadership the industry's challenges require.

Recommendation 10:

That the NZRB consider revamping its approach to the SOI process using it as a vehicle for industry-wide strategic dialogue and to produce a clear statement of strategic intent and planned outcomes (including financial targets).

Recommendation 11:

That, in consultation with the Codes, the NZRB revamps the CRIG mechanism to make it a more effective forum for industry leaders to conduct a continuous strategic dialogue.

4.4 Conclusion

The examples illustrated at the beginning of this part appear to be typical of a pattern established by the NZRB since its inception to ensure that its objectives, advocacy and decisions are well founded on thorough research and analysis. In addition, significant investment has been made by the NZRB in information systems generally (see Section 2) to

³⁷ There seems to be a widespread assumption that the present, multi-component structure of the industry cannot work. Conceptually, however, there is no reason why what is often called a 'federal' structure cannot be an effective one notwithstanding the inherent paradoxes of power and control contained within a federalist system (e.g. the need to make things big by keeping them small; to encourage autonomy but within bounds; to combine variety and shared purpose, individuality and partnership, local, regional, national and global, etc). Large, international businesses have been forced to learn how to manage such paradoxes in order to obtain the undoubted benefits of a federal structure. In the racing industry different organisational components (e.g. NZRB, codes, and clubs) need to link closely to create economies of scale but individually need a degree of autonomy because each has a particular competence and sphere of knowledge and because autonomy encourages ownership and releases energy.

It has been suggested that there are five basic principles of federalism (Charles Handy (1995) *Beyond Certainty*. London, Hutchinson. Chapter 3: 'Balancing Corporate Power: A New Federalist Paper'). These, on the face of it, seem very applicable to the racing industry in New Zealand:

1. 'Subsidiarity' – power is best exercised at the lowest possible point in the 'organisation' commensurate with functional competence (e.g. the NZRB should not do what the codes can do better; the Codes should not do what the clubs can do better).
2. Instead of higher levels attempting to 'steal' subordinates' decisions they should instead focus on assisting subordinates, by training, advice, and support, to make better decisions.
3. Subsidiarity is not the centre giving away or delegating power. Power is assumed to lie at the lowest point in the organisation and can be taken away only by agreement.
4. To be effective, subsidiarity has to be formalised. There have to be negotiated contracts that set the boundaries of each component's powers and responsibilities. One useful definition of corporate governance in this context is that it is the 'assignment of decision-making responsibility'. There needs to be clarity between the NZRB, the Codes and the clubs as to who can do what and whose authority counts where.
5. Subsidiarity requires intelligence and information. If people are to exercise their responsibility taking account of the interests of the whole, they must have both the information that allows them to do so and enough training and knowledge to interpret the information.

ensure that the industry has a solid basis for determining the changes it needs to make. This represents a significant improvement in performance over that achieved by the antecedent authorities.

Objective setting and the effective implementation of strategies to attain such objectives do, however, require more than effective data collection and thorough analysis. The description of the strategic and business planning processes outlined in this section indicates that process improvements are both possible and desirable. Such improvements would not only produce gains in transparency and accountability but would be important initiatives towards the integration and cohesion of the industry.

5 The Nature and Content of Policies and Strategies Intended to Achieve the Objectives

5.1 Introduction

This Part deals with the nature and content of policies and strategies intended to achieve the NZRB's objectives.

'A policy' can be thought of as an agreed basis for action that embodies an organisation's values and perspectives. Policies reflect important principles and mandate (or restrict) certain actions or behaviours that might be applied to the achievement of an organisation's objectives. Policies are an important component of an organisation's approach to realising its strategic intentions and provide an additional dimension of the accountability framework by establishing a basis for compliance.

'Strategies' are the means (activities, actions, programmes, projects etc) by which the organisation goes about achieving its objectives.

5.2 The Nature of NZRB Policymaking

From its earliest meetings the board has dealt with a range of policy issues, and there is now a well developed policy framework to guide the NZRB's operations. Policies are drafted by management and approved by the board. A number of these receive detailed consideration at the applicable board committee. For example, the Compensation and Development committee deals with policies and strategies that deal with the people side of the business (e.g. incentive structures).

Each policy is scheduled for regular review and may also be reviewed outside that schedule as necessary. At the present time a number of policies have been, or are in the process of, being deleted or incorporated into other policy documents.

Generally policies conform to a well structured, well thought out template which clearly states each policy's application, purpose, philosophy and objectives, definitions, and authorities. Procedures are also included where applicable.³⁸ Penalties for breaches of policy are also stated where appropriate.

Each policy is accessible via the NZRB intranet. A list of current policies listed on the intranet is contained in Appendix 4.

The current policy framework reflects a mix of 'law' (i.e. statutory requirements), 'lore' (i.e. customary practice) and 'guidelines' (e.g. dress code). There is recognition within the

³⁸ *Procedures* are documented activities described in sufficient detail that a person with relevant knowledge, skills and abilities but without in-depth familiarity of the activity can perform the activity.

organisation that there is room for improvement and the NZRB is currently reviewing the overall policy framework and also its policy development and implementation process. Arguably, for example, there are too many policies and this has implications for awareness levels and policy compliance.

5.3 Risk Management

An important aspect of achieving an organisation's objectives is the management of the risks that might be a barrier to, or even undermine, the achievement of organisational objectives. A comprehensive policy framework is very important in providing an overview of risk across the organisation and a significant proportion of the NZRB's policies are risk-related. Given the nature of the racing industry, it would seem to be appropriate to place a high premium on effective risk management.

Risks are identified incidentally in the normal course of the board's work through, for example, reports and proposals put to it. 'Routine' operational reporting to the board also identifies and highlights a range of risk issues.

The board's Audit and Finance Committee has experienced a growing role in relation to risk management. The committee's current annual work programme addresses:

- **Risk Profile.** This includes the requirement to review, monitor, assess and make recommendations to the full board of the NZRB on the NZRB's business risk management policy, risk appetite and risk management framework, including the adequacy of the organisation's overall control environment and controls in areas representing significant financial and business risk.
- **Risk Events and Incidents.** This includes the requirement to review, monitor, assess and make recommendations to the full board of the NZRB on the organisation's system of key internal controls including financial controls, fraud prevention controls, legal violations and non-compliance with the NZRB's Code of Conduct.

Under its auspices there is currently a review in progress of a wide range of risks including:

- risks that are 'generic';
- risks that could affect operational continuity; and
- reputational risk.

Risk management has been progressively strengthened at an operational level as well. For example, in 2007 a new management position – the Head of Risk, Legal & Audit – was established to provide a particular focus to risk at a senior management level. This third level position has 'dotted line' access to the Chair of the Audit and Finance Committee and the Chief Executive. Additional resource has been added since this position was established. One of the functions of this role is to enhance the risk management 'toolkit' available to the board and management. The Head of Risk, Legal & Audit chairs an executive risk

management committee (ERMC) that is responsible for the continual evaluation of risks and their management.

The function of the ERMC is to act as a forum to ensure adequate awareness and debate of all significant risk issues that face the NZRB in regard to Operational Risk and Compliance. The ERMC is responsible for ensuring systems and processes are in place for the early identification and appropriate management of risks facing the NZRB. The ERMC receives reports designed to provide it with the information necessary to discharge its responsibilities. Each Business Unit, by rotation, is required to provide an annual (or half yearly as required) report of its specific risk issues for discussion at each meeting. The ERMC reports (via the Risk Manager and/or the Chief Finance Officer) significant risk issues to the Audit and Finance Committee.

There is an operational risk management framework which is reported to the Audit and Finance committee as well. The Committee receives reports on progress on implementation of the framework.

In addition, the Audit and Finance Committee receives advice from the NZRB's external auditor, Deloitte, on Enterprise Risk Management (ERM). In a report to the board in July 2007 Deloitte described the four key drivers of ERM:

- governance (objectives, values, and policies)
- process (the activities that together produce a result of value to a customer or stakeholder)
- people
- technology

This is a useful framework for the board to consider when evaluating the effectiveness of risk management in the organisation. Broadly speaking, like other areas of policy in the NZRB, those relating to risk management tend to be staff-driven. While competent operational level risk management is essential, it is not a substitute for the board thinking for itself about risk. In an important Australian review of corporate governance in that country some years ago it was proposed that:

*The Board's key role is to ensure that corporate management is continuously and effectively striving for above average performance, taking account of risk.*³⁹

This underlines the important role a board has in determining the degree of risk that is acceptable. The board has (or should have) a different vantage point than management when it comes to thinking about risk. This requires a regular and continuing commitment at a governance level to characterise risk and ensure that appropriate policies and strategies are in place to manage and mitigate risk whether or not these are directly controllable by the organisation.

³⁹ Fred Hilmer (Ed.) (1998) Strictly Boardroom: Improving Governance to Enhance Company Performance. Melbourne, Information Australia. 2nd ed. Page 32.

Therefore, notwithstanding the work done on its behalf by the Audit and Finance committee, the board as a whole should conduct an annual discussion about risk management.

Recommendation 12:

That the board schedules an annual discussion of risk.

5.4 Delegation

A useful definition of corporate governance is that it is ‘the assignment of decision making rights’. Decision making authority lies with the governing board until such time as it delegates to the Chief Executive or other agents. Such delegation should be explicit and transparent. At the NZRB, the stated purpose of delegated authorities is:

- to have effective controls in place to minimise the risk from unauthorised expenditure, to ensure managers can control the amount to which their subordinates can spend and maintain control over budget spending.
- to formalise employees’ approval limits, clarify staff responsibilities, and provide a clear audit trail of staff delegation.

The most important delegation is arguably a financial delegation. The NZRB Delegated Financial Authorities (DFA) Policy is very comprehensive and covers delegations for capital expenditure, general expenditure and industry and statutory payments. It is reviewed annually. The most recent review was tabled and approved at the March 2008 Audit and Finance Committee meeting for recommendation to the board. This policy links closely to other pertinent policies including: the Contracts Policy, the Asset Management policy and the Purchasing and Procurement policy. A recent amendment of the policy was to provide for cover of delegations during a crisis (e.g. if the Chief Executive and Chief Operating Officer were not available to perform their duties during a crisis).

In recent years, significant attention has come to be placed on ‘sensitive expenditure’ in many types of organisations but particularly those, like the NZRB, in the public eye. The delegation framework covers areas like the use of credit cards. However, there may be value in a close review of the Auditor-General’s guidelines in this regard to ensure that the delegations cover all the bases.⁴⁰ There does not appear to be a formal delegation, for example, relating to the approval of Chair/members’ expenses.

Non-financial delegations (e.g. in relation to HR and Communications) are contained in the respective policies and procedures.

⁴⁰ Office of the Auditor-General (2007). Controlling Sensitive Expenditure: Guidelines for Public Entities.

5.5 The Development of Strategies

Since its formation, the NZRB has formulated a wide range of strategies intended to deliver its objectives and improve the efficiencies and effectiveness of various aspects of its functions. The approach adopted in this audit has been to examine a sample of strategies to form a view on the reasonableness of the approach adopted. It would be inappropriate for an auditor to substitute his/her judgment for that exercised by those accountable for making decisions, and to do so after the fact. The following strategies were selected for the purpose of this examination.

5.5.1 Channel Migration

During the period 2005/06 the NZRB investigated a number of strategies intended to improve the efficiency of its non-retail sales channels by encouraging wagering through the most cost-effective channels and to stimulate growth in the revenue achieved through those channels. Central to that analysis was an examination of the profitability of the Operator Assisted Phonebet channel, at that time the most expensive of the non-retail channels.

A detailed analysis of a range of options was undertaken. A consultation process was also undertaken to more fully understand the issues and potential solutions. As a consequence of work undertaken in the early stages of the project, the need for further analysis was identified and undertaken to progressively increase the level of confidence in the proposals formulated. During the course of what seems to have been a very deliberate and iterative process, consideration was given to a wide range of matters including:

- capital investment requirements
- business risk (including business continuity, impact on cashflow and profitability)
- the capacity of other channels to cope with expected migration
- technology capacity and capability, etc
- legal issues
- comparison of the experience of similar initiatives in Australia
- impact on staff
- impact on customers
- the economic and social impact on centres that could be affected (e.g. by rationalisation of existing facilities)

Assumptions were articulated and detailed sensitivity analysis undertaken on business projections.

As the final proposal took shape, the board was kept informed about the results of the various analyses and the developing thinking of the executives concerned. If anything, it might be argued that the board was presented with far more detail (including, for example, detailed consultant reports, etc) than was needed to form a governance level of view on the work undertaken and on the recommendation finally presented to introduce a \$5 minimum bet.

This was no doubt a decision of considerable significance and justified detailed analysis that the board, correctly, was made aware of. However, the board's job was, in all likelihood, more difficult than it needed to be, because it is likely that the detail of the papers would have made the matters of governance significance, more difficult to discern.

5.5.2 The Internationalisation Strategy

A multifaceted Internationalisation strategy has been developed. It was recognised that additional annual earnings were available to the NZRB from exploitation of opportunities across four areas of activity:

- expansion of New Zealand races into the Australian wagering schedule
- expansion in Australian races within the New Zealand wagering schedule
- international exploitation of New Zealand broadcasts with Sky Channel as the agent
- co-mingling (pooling) of:
 - NZRB bets on Australian races with Tabcorp;
 - Tabcorp bets on New Zealand races with NZRB; and
 - potential introduction of different bet types by NZRB

It was also recognised, however, that co-mingling with Tabcorp would not, in isolation, drive the most significant financial benefits for the NZRB but it would provide a vehicle to unlock opportunities to grow wagering. Co-mingling was expected to improve liquidity to all pools but to be most beneficial at the time of very weak pools (e.g. Tuesday night import greyhounds). From a Tabcorp perspective, co-mingling was expected to support their objective of having the NZRB import more Australian product. Tabcorp also expected the success of co-mingling would help encourage changes to the domestic New Zealand calendar to provide product at times suiting their schedule.

The move to a co-mingled market in 2007 was expected to considerably enhance the core TAB business proposition by providing more product, larger betting pools and increased quality of racing. However, the development of complementary sub-strategies was also important to support and deliver the benefits of the Internationalisation strategy to different stakeholder groups.

Changes to the domestic racing calendar

Changes were proposed to the domestic calendar in order to generate domestic turnover benefits, provide greater export commissions and open import opportunities to deliver consistent Australian product. This was the subject of considerable consultation with Code management. A calendar template was developed that details days on which domestic meetings are required and assumes the number of races each Code can sustain. This offered a framework for Codes to develop their domestic calendar with greater certainty of the NZRB's ongoing requirements. The development of this strategy has also been a catalyst for Codes to think beyond the objectives of their own racing preferences to the interests of the racing industry as a whole. Individual Codes benefit from a coordinated racing schedule that helps grow a bigger overall NZRB financial surplus.

The provision of more consistent imports

Previously, the NZRB brought limited, 'fractured' Australian meetings and carnivals to wagering customers. This poor coverage incentivised New Zealand domiciled customers to wager directly through Australian operators. The new domestic template allows the NZRB to provide more consistent import product, especially on Wednesdays and Saturdays. Import turnover has shown significant improvement over previous budget estimates.

The development and implementation of the Internationalisation and related strategies has not been easy. There were significant implications for the New Zealand racing and wagering industry given very strongly held beliefs and trained behaviours of codes, clubs and punters. For example, the selling of a single race with appropriate lead-in and vision coverage of the horses, racing form and provisional dividends was considered a fundamental right of every club. Punters, for their part, were never asked or educated to think beyond the next race. These strategies required a fundamental change in how the NZRB thinks about and delivers its vision, form and wagering data on both radio and television and for the Codes and clubs there was a need to alter their conviction about the nexus between funding and turnover.

5.5.3 The Go to Market Strategy

The Go to Market Strategy was developed in two stages. It began with customer segmentation research and the development of a segmentation model by rationalising five historical behavioural research projects. New customer segments were identified. This process was led by an external marketing agency with contributors from the NZRB and an international sports marketing consultancy.

Secondly, a 'Go to Market' strategy was developed. This refined the model to produce a number of strategies and tactics to engage prospects and customers in wagering with the TAB. The strategy focused on realistic initiatives that the three 'pure' segments ('Wont Bet Enough,' 'Cant Bet Enough' and 'Don't Bet Enough') developed in the original customer segmentation paper may not have clearly defined. The basis of the strategy developed was that there are two broad ways to drive growth:

- extract incremental growth from the current customer offering
- come to the market with a new offering to develop new customers/share

A key assumption in the development of the strategy was that the NZRB required strong growth over the next five years (from 2006) to see the NZRB on the path to turnover in the vicinity of \$2 billion by 2011. To do this there was a belief in the need for a 'revolution' in the offering, not simply an 'evolution'. Evolution was expected to bring good returns but insufficient alone to achieve the sustained growth required.

Opportunities for incremental gains were identified as being available through a number of initiatives (e.g. lifting the image of the retail network, building more modern and inviting stores, national promotions with aspirational prizes, etc). However, the NZRB research suggested that to make a true step-change in turnover it would need to offer the market a

proposition that brought new customers or a combination of new customers and more frequent betting from a large number of customers who are currently infrequent bettors.

It was assumed that real growth would be difficult to achieve in wagering on either side of the Tasman, and that businesses that have managed to bring a wider range of gambling propositions to customers have generally created more opportunities for growth.

5.5.4 The Retail Strategy

Prior to 2006 the business emphasis had been on growing the low-cost channels (Touch-tone and Internet). The development of the Retail Strategy focused on meeting the needs of TAB customers who currently place some or all of their bets at Retail. These customers are broadly the 'do bet' segment identified in the Go to Market Strategy. Key components of the strategy included:

Network Planning

This was based on assessing a catchment's potential at both the macro and micro levels, taking a systematic approach to identifying better locations and new outlet opportunities. This revealed the significance of a catchment's traffic at the macro level and the impact of factors such as car parking and visibility at the micro level. Decisions on site locations and formats are intended to be criteria driven.

Customer Engagement

Under-investment in the retail network and outlet fit-outs has directly contributed towards a negative TAB image with current and potential customers. Also, current trends, particularly in sports betting, are not well catered for in the present TAB layout and facilities. To address this issue, a network tiered refurbishment programme was adopted. A variety of initiatives were identified to improve the customer experience.

Retailer Engagement

A variety of initiatives were identified to improve retailer engagement, including improved facilities to help retailers' operations and improved incentives. These changes are also intended to build a platform for more viable and desirable retailer investment opportunities in the future.

Gaming Positioning

Strategies were developed around improving relationships with racing friendly trusts and working with retailers hosting gaming to develop a wider entertainment offering to appeal to more customers. In addition, the need to proactively lobby territorial authorities ahead of impending policy reviews was identified.

Back Office Support

Strategies focus on improving the organisation's ability and efficiency in getting data (promotional information, training records, performance reporting, etc) to and from retailers.

New Business

While a substantial part of the Retail Strategy is addressing past under-investment and shortcomings in the existing network, alignment with the Go to Market initiatives for new business is also recognised as critical.

5.5.5 Brand Portfolio Strategy

The NZRB Brand Portfolio Strategy was also examined. The primary goal of this strategy is to enable the TAB brand to be positioned in the minds of customers and stakeholders as a provider of competitive event wagering services and information. Secondary goals include aligning the TAB brand with the racing event content provider brand (Trackside) and the differentiation of the TAB and NZRB brands (the latter positioning itself as the provider of racing industry and wagering governance for New Zealand). The NZRB brand is uncontested whereas the TAB operates in a competitive market.

It is acknowledged within the NZRB that the development of the Brand Portfolio Strategy has underlined the critical importance of the organisation's culture and mindset. The necessary starting point is devotion to the desired customer experience. Development of the strategy also stressed the importance of the strategic business planning process for ensuring that every aspect of the business is aligned with the delivery of the core strategies. The need for substantial investment in Information Technology was also underlined. The strategy contains a detailed and extensive action list.

5.5.6 Possible strategy gaps

This aspect of the audit has not been designed to identify missing parts of the NZRB strategy. However, in contrast to other comparable industries, there does not seem to be a discernible 'industry good' strategy. In the dairy industry, for example, there is both a dedicated and relatively predictable funding stream for research and development, industry training, and the like, and an institutional infrastructure for applying that funding and delivering results. Industry training, for example, is particularly important if the racing industry strategy roll out requires significant mind shifts and up-skilling. During this audit, the NZRB was able to demonstrate that there has been increased expenditure and a number of industry good initiatives have been taken or are underway. In the absence of an integrated industry good strategy (covering both equine and the greyhound codes), however, there is a risk that these initiatives could be somewhat isolated and ad hoc and, therefore, do not achieve what they might.

5.6 Conclusions

To be effective a policy framework must be understandable, credible and accessible to those who must implement policies and comply with them. Otherwise the policies might as well not exist. Executive staff responsible for the oversight of the NZRB policy framework have a good understanding of the comparative strengths and weaknesses of the current policy

framework. As could be expected in any relatively new organisation, work is in progress to consolidate and strengthen the NZRB's performance in this area. There is now greater focus on this than there was in the early years.

As is appropriate to the industry, there is a widely based risk management infrastructure and this is still developing. The system for dealing with risk at a senior management level has been strengthened in recent times. While risk management has also been strengthened by increasing attention being paid to it by the Audit and Finance Committee, it is important that the board as a whole also has the opportunity to develop a holistic perspective on risk.

Effective delegation is a critical element of risk management and the NZRB has a comprehensive delegation framework for financial authority. The delegation framework is kept under review and is revised as necessary. While initiated by management this framework is approved by the board.

There is a comprehensive and discernibly thorough approach to the development of strategies to achieve the organisation's objectives. Systematic research, consultation and technical analysis have been features of the process of developing key strategies. The need for this may not always be apparent or understood, however, by stakeholders like the Codes. A number of Code representatives expressed a degree of frustration at the time taken for important strategies to be formulated and deployed. To the extent that such criticism is justified and is not simply a matter of inadequate communication, this may reflect a more fundamental resourcing issue. As noted earlier in this report there is a need for the NZRB and the industry to get 'better faster'. However, the NZRB does appear to be very dependent on a small number of key executives and their focus, to date, appears to have been primarily on the revenue generation (wagering and distribution) side of the business. While there is a variety of strategies being developed in these areas neither 'infrastructure' nor 'integrity', the other two key strategic 'pillars' have nominated senior executives in charge. Executive responsibility for those matters is dispersed among the whole senior executive team. The NZRB acknowledges the significant challenge it faces in recruiting the skills and experience it needs to advance its various strategies in these and other areas.

6 Monitoring and Implementation of Policies and Strategies

6.1 Introduction

The old adage that ‘what gets measured gets done’ highlights the importance of clarity in what *should* be measured and the quality of information received by a board to aid in the use of that data for monitoring. Reporting quality is possibly the most crucial ingredient in good governance and is central to the purpose of this part of the report which deals with the process and framework for monitoring implementation of policies and strategies. This has involved an assessment of whether the board has an effective and efficient monitoring system for ensuring that policies and strategies are implemented as intended and, to the extent that they are/are not, that there is an appropriate feedback loop resulting in necessary improvements.

6.2 Sources of Monitoring Information

To undertake its monitoring function a board relies on information from a combination of three principal sources:

- Executive reports
- Its own direct observation of the business
- Independent third party reports (e.g. audit reports)

6.2.1 Executive reporting

For their understanding of the way the business is tracking and the effectiveness of policies and strategies, most boards rely primarily on reporting from the chief executive and other senior executive sources.

At most meetings the NZRB board receives ad hoc reports about significant issues which are strategic at organisation and/or industry levels which enable it to form a view on how such matters are being handled and progressed. Recent illustrations, for example, include reports on the handling of the Australian equine influenza crisis.

Overall business performance is reported monthly and, as a matter of routine, the board also receives reports updating progress in relation to key strategic initiatives. In recent months such reports have dealt with, for example, progress in relation to infrastructure initiatives. These reports occupy the front of the board paper pack and the initial agenda items and therefore take up time during the most productive part of the board meeting. It is typical, however, that such reports deal with matters in some considerable operational detail. These reports do not usually articulate the reason for drawing these matters to the board’s attention

and, consequently, what consideration/action, if any, is required of the board. It is often difficult to judge whether the information is supplied from a 'nice to know' or a 'need to know' perspective. Much of the content of recent board papers would seem to be 'for (general) information' rather than 'for action'. It could be argued that while such reports are styled as 'strategic' they do not, therefore, assist the board to assess matters at a level applicable to the governance role.

Viewed in its totality, the greater part of the information reported to the board each month, is from divisional managers and relates to issues and activities specific to their functional responsibilities. The content and formatting of these reports is inconsistent between different authors and does not assist members to tie information provided to them back into key strategic objectives. As a consequence, the perspectives of the organisation's operational 'silos' tend to dominate the raw material on which members rely in their preparation for a board meeting.

A notable absence is an overview or synthesis that would help the board take a helicopter view of the business. The financial report provides a high-level overview of a sort but, by its nature, such a report is about past events and the financial performance of the business is usually a consequence of the effectiveness and efficiency of other aspects of organisational performance.

In the NZRB, the Chief Executive's report which might provide this overview tends to deal with progress reporting on an ad hoc range of issues not covered in other reports. Both in subject and content these are often operational in nature as well. The board would benefit by receiving a coherent, high level overview of the way the business is tracking against the key strategic imperatives of the business. Such a review should be formatted to focus on whether actual outcomes (including targets and, where relevant, project milestones) are being achieved.

Recommendation: 13

That monthly board papers contain a high level overview report from the Chief Executive that highlights strategic issues for the board's attention and summarises progress against the key elements of the 'strategic plan'.

What is reported to a board for monitoring purposes should be able to be explicitly linked to pre-agreed strategic or policy objectives and related performance indicators. The performance management framework should contain 'leading' (i.e. future oriented) as well as 'lagging' (historical) indicators. In the current business performance update provided each month within the Chief Operating Officer's report, the performance indicators are essentially lagging indicators. They tell the board what has happened in the business (and in the Codes) after it has happened. That approach is a valid aspect of board reporting but it is notable that variances reported in Code-related performance areas are comparisons between 'this year' and 'last year' rather than between 'actual' and 'planned' performance. The latter is a more powerful basis for performance management.

Information in the ‘nice to know’ category also fulfills an important role but it need not be provided to the board via the monthly board papers. For example, a former chief executive of the TAB disseminated such information via a weekly newsletter styled the ‘Friday Flash’.

A useful discipline to help identify what should be in board meeting papers, as opposed to some other medium, is to preface every report with a reference to a board-relevant policy or strategic objective. This is a pragmatic criterion for determining what should be going to the board and also has the benefit of requiring the board to be specific about its reporting requirements.

Most reports to the board are primarily *management* relevant reports that relate to operational functions and management activities rather than *governance* reports that relate to the board’s interests in progress against the achievement of strategic objectives. This is most likely a consequence of the absence of a clearly stated strategic plan which was referred to earlier in this report.

A number of board reports reviewed made good use of visuals (e.g. graphs) to summarise and aid interpretation of numeric data. However, it is relatively uncommon to use this technique in relation to the performance monitoring reports prepared for the board. The one-page Treasury report which combines graphs with ‘snapshot’ data tables is a good model.⁴¹ The ‘traffic light’ format adopted in the IT project progress report is also a good model worthy of wider application. Both approaches help draw board members’ attention to those matters deserving of their attention at a governance level while at the same time offering additional information should individuals wish to ‘drill down’.

While this section has contained a relatively critical analysis, the executive reporting situation described is common in all but a small proportion of organisations in New Zealand and Australia. While increasing attention has been paid in the last 10 to 15 years to the professional development of boards and directors, it has been largely overlooked that a significant factor in board performance is senior executives’ ability to provide appropriate professional support to their board. They also have ‘governance’ training needs. Nowhere is this more important than in the preparation of information for governance purposes. Simply passing reports prepared for management purposes on to the board is neither efficient nor effective. Board time (including members’ preparation time) is too precious to spend wading through reports that were not prepared for the purpose and which do not assist members, individually and collectively, to get directly to the nub of organisational performance.

Recommendation 14:

That executives reporting to the board receive appropriate training to support any changes agreed to the board reporting regime (see also Recommendation 7).

In the early years, a running list of agreed/requested actions was maintained and reported to the board but this is no longer in evidence. This makes it difficult for the board to track progress in relation to its decision making.

⁴¹ Board meeting papers, 18 March 2008, page 64.

Recommendation 15:

That an 'actions to be taken' list is prepared to supplement board minutes.

6.2.2 Third party reporting

Without implying any distrust of, or disregard for management, there are some matters that require inputs or perspectives management cannot provide or a degree of independence that management does not have. Sometimes a board must validate management information or actions or even seek 'another opinion'.

The external audit process is a common example of independent third-party assessment of organisational performance albeit that the scope of a typical annual audit may be more narrowly based than some may wish. External auditors are, however, potentially a good source of independent advice about aspects of organisational efficiency and effectiveness.

Since the establishment of the NZRB there have been examples of third party reporting on matters going to the heart of the organisation's efficiency and effectiveness. The work done by the Boston Consulting Group in 2004 is a prime example.

It is always an option for the board to initiate an independent review of any aspect of organisational performance should it wish to get an external perspective.

6.2.3 Direct observation

In respect of significant aspects of performance monitoring the board must depend on its own assessment because it is the 'end user'. There is little point asking an external adviser whether, for example, the timeliness of board papers is satisfactory or whether board papers are understandable. Only the board can make that judgement.

Two of the board's committees are central to its ability to monitor organisational efficiency and effectiveness and undertake a lot of the detailed analysis. The Audit and Finance committee is particularly important in this respect because its role is to review, monitor, assess and make recommendations to the full board on:

- investment, asset divestment, and balance sheet structure,
- financial reporting and controls,
- risk management,
- internal controls, and
- audit (internal and external) functions

While the committee also relies to a substantial extent on management advice in fulfilling these functions its detailed scrutiny of these matters places it in a position to form a view

about the performance of the system in general and of management. This underlines the importance of careful selection of board members – particularly those who are nominally ‘independent’ – to ensure they have the experience necessary to form such judgements. The committee also engages directly with both internal and external auditors dealing with their recommendations on financial reporting, controls and other matters together with management’s response.

While this committee’s scrutiny (and that of the Compensation and Development Committee in relation to senior executive performance) is important, the board as a whole must take ultimate responsibility for effective monitoring of organisational performance.

6.3 Evaluation

Board and senior management attention in most organisations is focused on shaping and implementing important decisions. Almost as soon as any decision is made attention inevitably shifts towards the next challenge. As a consequence, there is typically little time or attention devoted to post-implementation review – checking actual outcomes against the original assumptions and decision making criteria as part of a conscious learning process designed to improve future performance.

Within the NZRB it is acknowledged that the undertaking of 'post implementation reviews' or 'benefits realisation reviews' of strategic decisions and/or of projects that have come about due to a strategic decision taken, is currently more an ad hoc than a systematic process. The organisation has, for example, undertaken reviews around the achievement of the planned benefits of moving the Phone Bet minimum to \$5 (and thereby closing the Palmerston North Phone Bet site). At the time of the audit the board was scheduled to receive an update regarding the achievement of the planned financial benefits derived from the Tabcorp Internationalisation project.

The NZRB has recently strengthened the Project/Programme Management Office and it is being moved to sit within the strategy area of the business. As part of the ongoing development of the PMO function there is intended to be a focus on formalising the post implementation process.

Among senior management there is a consciousness of the importance of post implementation review processes and these initiatives are progressively improving the organisation’s capability in this regard.

6.4 Conclusion

The board is not short of information for monitoring purposes. In common with many boards, in fact, it probably receives too much. It would benefit from executive reporting, in particular, being reshaped to give the board a greater sense of ‘overview’ and more of a focus

on the 'governance' dimensions of issues. This is a question of both content and presentation.

7 Conclusions and Recommendations

7.1 Overall Conclusions

Because of the importance of the New Zealand racing industry in so many different ways, the effectiveness and efficiency of the NZRB has great significance not only for racing industry participants, but for New Zealand generally.

Undoubtedly the NZRB has achieved much since its formation and it has many further initiatives 'on the boil'. Not least the NZRB has made major financial gains for the industry which are significant even when the effect of advantageous tax changes is excluded.

Key stakeholders such as the racing Codes are generally positive about the progress the NZRB has made, particularly in a financial sense, and understanding of the reasons why more progress might not have been made in some areas. The industry is far better informed about its essential characteristics (including its basic economics) than it was five years ago. The NZRB has adopted a disciplined, evidence based approach to the changes it has pursued. This inevitably takes time and some stakeholders are impatient for many important and as yet unresolved matters to be attended to.

The NZRB as a separate entity is still a relatively young organisation. It is an industry 'peak body' that operates in a comparatively fragmented and internally competitive institutional environment. In addition, the organisation, and the industry as a whole, operates in a dynamic global environment. Some of its functions are under intense competition. The status quo is not an option. The organisation must 'get better, faster'. This places a very high premium on good governance and management. Both governance and management performance have progressively strengthened during the first five years of the organisation's existence. Many of the organisation's basic governance and management systems are working well and producing good results.

Notwithstanding the undoubted progress that has been made, this report has also identified areas where further development and strengthening would be desirable. Such changes as have been recommended fall into the category of 'progressive incremental improvement' rather than 'requiring urgent remedial attention'. The changes recommended, while not major in themselves, are considered essential to enable the NZRB to deliver on its industry leadership challenge and to demonstrate the highest possible standards of governance for other entities in the industry to follow.

In particular, the NZRB's articulation of its strategic intent and strategic direction requires further development. It is vital that the NZRB take a lead in addressing significant remaining barriers to the wellbeing of the industry even though some of these matters are the primary responsibility of other components of the industry. Process improvements are also possible and desirable. Such improvements as have been canvassed in this report would not only produce gains in transparency and accountability but would be important initiatives towards the integration, cohesion and performance of the industry.

7.2 Summary of Recommendations

1. That an operational definition of 'independence' relevant to the NZRB be developed and applied by the nominations advisory panel in considering future board candidates.
2. That there is a thorough, 'first principles' review of the current conflict of interest policy.
3. That a board charter or terms of reference be developed to document the board's interpretation of its role and responsibilities and to serve as an accountability framework for the board and individual members.
4. That the board undertakes a regular self-assessment process covering the effectiveness of the board, the Chair and individual members.
5. That the board develops and implements an annual agenda setting process to give greater focus to key strategic issues.
6. That the board makes further changes in the structure of the board meeting agenda to improve the flow of board meetings and encourage a governance rather than operational focus.
7. That the board review the present pattern of board papers with the intention of having these recast to better align with the needs of the board for governance-related information (see also Recommendation 13).
8. That the governance statement in the annual report is expanded to provide more information on governance challenges, structures and processes and that it and related material be accessible via the web-site.
9. That the NZRB consider revamping its business plan to better articulate planned outcomes (including project milestones and financial targets) and priorities and to facilitate more meaningful consultation with the Codes about both planned outcomes and strategies to achieve those outcomes.
10. That the NZRB consider revamping its approach to the SOI process using it as a vehicle for industry-wide strategic dialogue and to produce a clear statement of strategic intent and planned outcomes (including financial targets).
11. That, in consultation with the Codes, the NZRB revamps the CRIG mechanism to make it a more effective forum for industry leaders to conduct a continuous strategic dialogue.
12. That the board schedules an annual discussion of risk.
13. That monthly board papers contain a high level overview report from the Chief Executive that highlights strategic issues for the board's attention and summarises progress against the key elements of the 'strategic plan'.
14. That executives reporting to the board receive appropriate training to support any changes agreed to the board reporting regime (see also Recommendation 7).
15. That an 'actions to be taken' list is prepared to supplement board minutes.

Appendix 1: Terms of Reference

Background

The New Zealand Racing Board was established by the Racing Act in 2003. The Act requires that, at least once every 5 years, the Board must arrange for an audit to be conducted in relation to how effectively and efficiently the Board is performing its statutory functions. These functions are defined as follows:

- (a) To develop policies that are conducive to the overall economic development of the racing industry, and the economic well-being of people who, and organisations which, derive their livelihoods from racing;
- (b) To determine the racing calendar each year, and issue betting licenses, under Part 5;
- (c) To conduct racing betting and sports betting, and make rules relating to betting, under Part 6;
- (d) To distribute funds obtained from betting to the racing codes in accordance with sections 16 and 17;
- (e) To administer the racing judicial system in accordance with sections 36 to 41 and Schedule 3;
- (f) To develop or implement, or arrange for the development or implementation of, programmes for the purposes of reducing problem gambling and minimising the effects of that gambling;
- (g) To undertake, or arrange for the undertaking of, research, development, and education for the benefit of New Zealand racing;
- (h) To use its resources, including financial, technical, physical, and human resources, for purposes that, in the opinion of the Board, will directly or indirectly benefit New Zealand racing;
- (i) To keep under review all aspects of racing and to advise the Minister of those aspects, either on its own initiative or at the request of the Minister; and
- (j) Any other functions that it is given by or under this Act or any other Act.

In carrying out these functions, the Board must also:

- Comply with the principles of natural justice.
- Exhibit a sense of social responsibility by having regard to the interests of the community in which it operates.

Conduct of audit

Scope

In determining the Board's performance and efficiency, the person appointed to conduct the audit must take into account:

- (a) the extent to which the Board has established objectives for the performance of its functions;
- (b) the nature of those objectives;
- (c) the progress the Board is making towards the achievement of those objectives;
- (d) the extent to which the Board has put in place policies and strategies to use its resources effectively and efficiently for the purpose of achieving those objectives;
- (e) the nature of those policies and strategies, and the manner in which they were put in place; and
- (f) any other matters determined by the Board.

While the Act states that audit must relate to the Board's performance on the particular day on which the audit is conducted, and its prospective future performance, the person conducting the audit may also have regard to the Board's performance during the 5 years before that day.

The audit will examine, verify and, if appropriate, validate, the steps the Board has taken to date and recommend any further steps the Board should take to ensure that it is well positioned and capable of discharging its functions.

Consultation

The Board has consulted recognised industry organisations in the preparation of these Terms of Reference.

Appointment of auditor

To conduct the audit the Board is required to appoint a suitably qualified and experienced person who may not be a member, former member, or employee of the Board. The Board envisages that such a person would have relevant experience in the corporate governance of statutory and similar entities and, in particular, in the evaluation of the performance of governing boards.

Reporting

The person who conducts the audit must, after conducting it:-

- (a) prepare a written report on the conclusions reached as a result of the audit; and
- (b) provide copies of the report to the Minister, the Board, and the recognised industry organisations.

Fees and expenses

The Board will pay the reasonable costs of the audit to the person who conducts it in terms of fees and the reimbursement of expenses. The Board will ensure that the person appointed will be supported in the conduct of the audit by way of access to information and personnel and the provision of administrative support when requested.

The Racing Board's contact point for this purpose will be:

David Walsh
Chief Operating Officer

Appendix 2: Consultations

Michael Stiassny	Chairman, New Zealand Racing Board
Thayne Green	Board member, New Zealand Racing Board
Liz Dawson	Board member, New Zealand Racing Board
Julie Crengle	Board member, New Zealand Racing Board
Ray O'Connor	Board member, New Zealand Racing Board
Alistair Sutherland	Board member, New Zealand Racing Board
Warren Bell	Board member, New Zealand Racing Board
Graeme Hansen	Chief Executive, New Zealand Racing Board
David Walsh	Chief Operating Officer, New Zealand Racing Board
Michael Wemyss	Head of Risk, Legal & Audit, New Zealand Racing Board
Anthony Crummy	Head of Strategy, New Zealand Racing Board
Guy Sargent	Chairman, New Zealand Thoroughbred Racing
Campbell Moncur	General Manager, Business Development, New Zealand Thoroughbred Racing
Simon Cooper	General Manager, Communication. New Zealand Thoroughbred Racing
Trevor Deed	Chairman, Greyhound Racing New Zealand
Jeremy Kennerley	Chief Executive, Greyhound Racing New Zealand
Pat O'Brien	Chairman, Harness Racing New Zealand
Edward Rennell	General Manager, Harness Racing New Zealand
Dudley Brown	Chief Executive, Equine Industry Training Organisation

Appendix 3: Industry Roles and Responsibilities

(Source: NZRB)

	NZRB	Code	Club
Governance	Industry Oversight Strategic Direction Business Planning R&D and Education	Rules of Racing Code Strategies Business Planning	Support & Implement Rules Club Strategy Business Planning
Integrity	Framework & Minimum Standards JCA Problem Gambling	Infrastructure Enforce Rules of Racing	Facilities & Resources
Calendar	Dates / Licenses	Pattern Racing Ratings / Gradings National Programme	Event Management Field Optimisation
Funding	Prudent Financial Management Distributions	Club Distribution & Stakes Policies Administrative Efficiency	Takes Optimisation Venue Efficiency
Promote Wagering & Racing	Participation Strategies Marketing (Wagering) Channels Betting Options	Ownership Programmes Marketing (Animals/Code) Stud Book / Licenses / Bureau	On-Course Amenities Event Promotion

Appendix 4: Current policies

The following are policies listed on the NZRB intranet as at May 2008. (Note that a small number of these have been/are in the process of being deleted or incorporated into other policy documents.)

- Accounting Guide - Retention of Business Records
- Accounting Policy - Petty Cash (Number 5)
- Accounting Policy - Purchasing (Number 3)
- Accounting Policy - Staff Expenditure Claims (Number 6)
- Corporate Governance - Compliance Manual
- Corporate Governance - Legal Library
- Corporate Governance Policy - Harm Prevention & Minimisation
- Corporate Governance Policy - Privacy Act
- Corporate Governance Policy - Risk Management
- Corporate Governance Policy - Security
- Corporate Services Policy - Application for DFA
- Corporate Services Policy - Asset Management -Short Capex form
- Corporate Services Policy - Asset Management
- Corporate Services Policy - Contracts
- Corporate Services Policy - Corporate Credit Cards
- Corporate Services Policy - Delegated Authorities
- Corporate Services Policy - Treasury
- HR Guideline - Managing Poor Performance
- HR Policy - Cell Phone Use Policy
- HR Policy - Departures & Exit Policy
- HR Policy - Dress Code
- HR Policy - Education Support Programme
- HR Policy - Employment of Family Members
- HR Policy - Employment of Former Staff Members
- HR Policy - Harassment Prevention
- HR Policy - Health & Safety Policy and Procedures Manual
- HR Policy - Health & Safety
- HR Policy - International Business Travel
- HR Policy - Leave
- HR Policy - Long Service Recognition Policy
- HR Policy - Phonebet House Rules
- HR Policy - Recruitment and Selection
- HR Policy - Smoke Free Environment
- HR Policy - Social Clubs and Associated Events
- HR Policy - Staff Betting

- HR Policy - Succession Planning
- Legal Compliance Guide - Employment Relations Act 2000
- Legal Compliance Guide - Fair Trading Act 1986
- Legal Compliance Guide - Financial Transactions Reporting Act 1996
- Legal Compliance Guide - GST Act 1985
- Legal Compliance Guide - Health and Safety in Employment Act 1992
- Legal Compliance Guide - Privacy Act 1993
- Legal Compliance Guide - Protected Disclosures Act 2000
- Legal Compliance Guide - Racing Act 2003
- NZ Racing Board Staff Handbook July 2007
- Operational Policy - Sports and Race Fixed Odds Betting Policy
- Technology Policy - Internet
- Technology Policy - Personal Computers