

“New Business Models and the Regulatory State: A Retail Case Study of Betting Exchanges”

AUTHORS	Peter Jones David Turner David Hillier Daphne Comfort
ARTICLE INFO	Peter Jones, David Turner, David Hillier and Daphne Comfort (2006). New Business Models and the Regulatory State: A Retail Case Study of Betting Exchanges. <i>Innovative Marketing</i> , 2(3)
RELEASED ON	Friday, 01 September 2006
JOURNAL	"Innovative Marketing "
FOUNDER	LLC “Consulting Publishing Company “Business Perspectives”



NUMBER OF REFERENCES

0



NUMBER OF FIGURES

0



NUMBER OF TABLES

0

© The author(s) 2024. This publication is an open access article.

NEW BUSINESS MODELS AND THE REGULATORY STATE: A RETAIL CASE STUDY OF BETTING EXCHANGES

Peter Jones, David Turner, David Hillier, Daphne Comfort

Abstract

New developments in Information and Communication Technologies, which have the potential to produce new business models and to transform the relationships between businesses and their customers, are posing challenges to the regulatory role of the state. Within the UK sports betting has traditionally been largely conducted in betting shops but the recent emergence of betting exchanges, which provide a virtual platform allowing customers to bet against each other rather than against the betting shop operator offers a new retail business model. This model has posed a threat to the betting shop companies, which has in turn led them to call for government regulation to provide fair competition and safeguards for customers. This case study examines some of the main issues raised in the debate between the betting shop and betting exchange companies about the need for, and the nature of, such regulation and includes a short outline contrasting betting shops and betting exchanges, a brief review of the literature on the role of the regulatory state and retail regulation and examination of the arguments put forward for and against state regulation of betting exchanges. More generally the case provides some empirical illustrations of the challenges involved in regulating new developments in Information and Communication Technologies and some more insights into the relationship between the state and retail capital.

Key words: Regulation, Betting Exchanges, Betting Shops, Information and Communication Technologies, State.

Introduction

Within capitalist societies the state has long been a major institution (Pierson, 1996) but as globalization has increasingly become the explanatory concept of economic and social change so the state has been seen to be in retreat as its authority has leaked away (Strange, 1996). At the same time recent and often rapid developments in Information and Communication Technologies, which have the potential to produce new business models and to transform and revolutionize relationships between businesses and their customers, are posing new challenges to the regulatory role of the state (Cranor and Wildman, 2002; Svantesson, 2005). Within the UK the betting shops have dominated the betting industry since the early 1960's and the state has played a major role in regulating, and taxing, betting shop operations. Betting shops look to offer customers a service namely the opportunity to strike a financial wager, or bet, with a bookmaker, or more generally with the firm owning the betting shop, on the result of an uncertain event, be that a horse race, a greyhound race, a football match or snow falling on Christmas Day. The recent emergence of a small number of betting exchanges, which provide a virtual platform, which in turn enables customers to bet against each other rather than against the betting shop operator offers a new retail business model for sports betting and poses a potential threat to the existing betting shop operators which has led them to call for government regulation to provide fair competition and safeguards for customers. This paper presents a short case study, which explores the contested perspectives on the role the state should play in regulating betting exchanges. The case includes a short outline contrasting betting shops and betting exchanges, a brief review of the literature on the role of the regulatory state and retail regulation, an examination of the arguments put forward for and against state regulation of betting exchanges and a brief discussion of the links between this debate and the literature on the role of the regulatory state.

The Regulatory Role of the State

Despite the increasing emphasis on globalization as the explanatory concept of economic and social change within capitalist societies the state still plays an important and diverse role in shaping business activities and environments. In conceptualising the role and function of the state in relation to business activities three broad categorisations can be recognised. A liberal pluralist perspective views the state as a neutral arbiter acting independently and working for the benefit of society as a whole. The Marxist, or political economy, perspectives are based on the belief that rather than being a neutral arbiter, the state reflects the deeper patterns of dominance and exploitation and that in capitalist societies it works to promote the interests of capitalists and capitalism. The third, neo-Weberian, perspective rejects the primacy of economic forces and seeks to identify ways in which the organisational structures and administrative procedures of the state affect business operations.

In their discussion of market structure and control within the retail sector of the economy Newman and Cullen (2002) argue that the government's most important role is as a policy maker but its role as a regulator has also attracted considerable attention. So much so that during the past decade research into retail regulation has become one of the key themes in the 'new retail geography' (Lowe and Wrigley, 1996). Writing in 1996 Lowe and Wrigley argued that academics studying retailing had been "remarkably silent about regulation and the complex and contradictory relations of capital with the regulatory state". Six years later the same authors (Wrigley and Lowe, 2002) were able to guide their readers through the debates and literature that had characterised a lively and theoretically informed interest in regulation during the intervening period. However Crewe (2000) has noted that a good deal of the work published on the relationship between the regulatory state and retailing has "remained empirically partial" in that it has focused upon the food industry and food retailing in particular and more generally upon the retailing of goods rather than services.

Within the literature referred to above two specific themes have attracted particular attention namely the operation of contested regulatory practices and debates about public interest versus private interest regulation. The work on contested regulatory practices has explored the ways in which these practices can shape business activities and has focused on the construction and implementation of regulatory practices and on how government and companies have exercised, shaped and contested regulatory frameworks and authority. Traditional models of regulation have centred on public interest regulation in which central and/or local government employs legislative controls and/or guidance frameworks, claims to operate in the public interest and are open to some form of public participation and scrutiny. In contrast private interest regulation is where the state empowers particular private sectional interests to act on its behalf to regulate the activities of other players and these voluntary processes are not subject to public participation or scrutiny.

Betting Shops

Gambling is probably as old as society and in the UK betting on sporting events, particularly horse racing has a very long history. Prior to the 1960 Betting and Gaming Act, betting legally on sporting events was only available at horse racing courses and greyhound tracks or via telephone credit betting services. For almost 40 years since then sports betting was focused on betting shops and increasingly dominated by a small number of betting shop chains. In many ways the passage of the 1960 legislation was both a recognition and a legitimisation of the substantial volume of illegal betting activity, organised by local bookmakers, which had existed throughout the UK since the late nineteenth century.

Betting shops look to offer customers a service, namely the opportunity to strike a bet and to experience the excitement associated with watching the event on which the bet has been struck. While individual private wagers can be struck orally, large scale betting operations catering for large numbers of customers require receipted transactions and precise record keeping. That said the act of placing a bet is simple and straightforward. The customer writes out a simple statement of his/her bet, for example 'Spring Cabbage' £10 Win' which is handed across a counter with the appropriate remittance

to a member of the betting shop staff who provides the customer with a copy of the bet that forms both a receipt and a record of the transaction. If the customer's bet is successful he/she returns the receipt to the counter staff who pay out the appropriate winning returns.

The UK's first betting shops were opened in 1961 and their numbers grew rapidly to some 16,000 by the end of that decade. Initially the market was fragmented and the majority of the initial outlets were owned and operated by independent local bookmakers who had taken the opportunity presented by the 1960 Act to trade legally. However over time marked concentration occurred as a small number of betting shop chains became increasingly dominant players and the total number of betting shops declined from 12,000 in 1980 to just over 10,000 a decade later and to an estimated 8,600 in 2005 when an estimated £33,700 million was staked generating some £2,834 million in net expenditure (Mintel, 2005a). At that time the market was dominated by five major betting shop chains namely Ladbrokes, William Hill, Coral, Stanley Racing and the Tote, which collectively accounted for some 65% of all outlets. Live horse racing and greyhound racing have traditionally been the major elements in betting shop business but more recently there has been considerable growth in betting on soccer, rugby, cricket, golf, tennis, virtual horse and greyhound racing and a variety of lottery style numbers games and gaming machines.

While the 1960 legislation permitted betting shops for the first time it also contained a strong regulatory element. Indeed in sanctioning and licensing betting shops the government was seeking to bring the illegal back street betting industry under regulatory control in the belief that as long as such activity was unregulated it could give rise to crime and cause social and financial problems to gamblers and their families. Further the general objectives in licensing betting shops were to prevent gambling from being a general source of crime or disorder, being associated with crime or being used to support crime; to ensure that gambling was conducted in a fair and open way; and to protect vulnerable individuals from being harmed or exploited by gambling. In order to open a betting shop an individual or a company had to apply for, or already hold, a bookmaker's permit and a betting shop license from the Betting Licensing Committee at the local Magistrate's Court. In granting such application the Committee had to be satisfied that the applicant was a fit and proper person, or organisation, to hold a permit, that the premises were suitable and that there was sufficient demand.

The clear message within the 1960 legislation was that betting should not be an enjoyable activity and that there should be no artificial stimulation to encourage people to bet. Betting shops were not to be situated on main roads with side and back streets considered to be more appropriate for this legitimate but still seemingly dubious activity. Internally such shops also originally reflected the spirit of the 1960 legislation and while they varied in their detailed characteristics the general picture was of a spartan and austere environment, which would not encourage customers to linger. From the 1970's onwards the introduction of more liberal legislation led to a more relaxed approach to betting shops and they have now become an accepted part of the high street and they offer smart interior designs and layouts and extensive live television coverage of a wide range of sporting events.

Betting Exchanges

The concept of betting on the exchanges is a simple one. Betting exchanges match up an individual who wants to bet on the outcome of an uncertain event at a given price with someone else who is willing to offer that price. The betting exchange has no interest in the outcome of the bet and simply acts as a broker, introducing customers to each other via the Internet, and holding the stake money to ensure that the winning customer gets paid. A customer has to register with one of the exchanges and makes a deposit, usually by credit or debit card, to allow them to bet. The exchange charges the winning customer a commission of up to 5%.

Betting on the exchanges is seen to offer a number of attractions. A customer can, for example, either have (place) a bet on a horse or a dog or an athlete to win a race or on a team to win a game or a competition or accept (lay) a bet if he/she thinks the horse/dog/athlete or team is going to lose

and the customer determines the price at which they enter the market. Customers can also place or lay a bet once a race or match has started and thus they can compete with each other on their ability to interpret how a race or match is progressing. Since the commission charged by the exchange is much smaller than the traditional betting shop chain's profit margin the prices on offer on the exchanges are generally more generous. One disadvantage is that there may not be sufficient people interested in laying bets on certain races or matches and, even when there are, the sums of money on offer may be very small.

Betting exchanges are relatively straightforward, though they do require customers to have access to a computer, to have at least basic computer literacy, to be registered with an exchange operator and to have a bank account. Once a customer has logged into a betting exchange web site, he or she selects a race or event, and a list of prices available at that time are displayed. If it is a bet on soccer's English Premier League, for example, the left-hand side of the screen displays the prices at which the customer can lay a team and the amount of money available at these prices, while the right-hand side displays the prices and the amounts at which a customer can back the team. The exchange will always highlight the best price available at that time. If the customer wishes to accept any of the prices available he or she simply clicks on the price available, and is then taken to a screen at which to enter the amount to bet or to lay. The amount the customer can win or lose is calculated and displayed, followed by an invitation to confirm the bet and all bets are set at multiples of £2 which is the minimum stake permitted. If the prices on offer are unattractive, the customer can post a price of his or her own on the exchange, and wait to see if any other customers are prepared to accept the bet.

In 2004-2005 betting exchanges were estimated to be generating £4,352 million in turnover within the UK (Mintel, 2005b). The major betting exchange company in the UK is Sporting Exchange Limited, trading as Betfair and it is estimated to have some 300,000 users and matches over a million bets per day during peak trading periods (Mintel, 2005b). The company was founded in 1999 and launched its web site in mid-2000. The company describes itself as the world's largest online betting organisation and claims to be "Revolutionising Betting". The web site claims that odds are consistently around 20 per cent better than those available from traditional bookmakers, and commission rates vary between 2 and 5 per cent on net winnings, according to a sliding incentive scheme depending on the amount staked during each month. In essence, the more the customer bets, the lower the rate of commission. Rates are adjusted and reported weekly, on the basis of past as well as current staking levels. All credit card details transmitted via the Internet are encrypted. While Betfair is widely recognised as the market leader there are several other betting exchanges including Betson, Betdaq, Intrade UK, Bet and Game and Betmate UK. The betting exchanges advertise extensively on the Internet, regularly in the specialist racing press, and also occasionally in quality broadsheet newspapers. National television coverage during UK Channel Four's racing programmes and "Morning Line" feature price movements on the betting exchanges as an integral part of the information they provide for viewers, which in turn has served to spread public awareness of this new style of betting.

In many ways the emergence of the betting exchanges has not only added a new dimension to sporting betting but it is also beginning to bring radical and fundamental changes to the betting industry. So much so that one commentator (Research and Markets, 2004) described betting exchanges as "the eBay of the Betting Industry" suggesting that they will "revolutionize" the betting industry and "change it forever." Within the world of horse racing, for example, one authority (Racing Economics, 2003) has argued that the growing strength of the betting exchanges is changing the landscape for wagering and radically altering traditional betting markets. Two immediate effects were identified namely that betting shops were responding by offering customers higher margin betting opportunities, as witnessed by the growth of fixed odds betting terminals, and that the contributions from on course bookmakers to the Horserace Betting Levy Board, which are distributed for the improvement of horse racing, are declining. More generally the growth of the betting exchanges has also improved the information flows to customers and while the on-course market has long been the traditional guide to the chances of a horse it is generally only formed

within 30 minutes or less of the start of a race whereas the prices available on the betting exchanges now offer similar information hours, and sometimes days, in advance of a race.

Contrasting Perspectives on the Regulation of Betting Exchanges

The rapid emergence of the betting exchanges has generated considerable debate concerning the need for, and the nature of, regulation and in part this debate has been focused in and around the development of the new Gambling Bill, which passed onto the statute books in 2005. This debate centred on a range of partly inter-related issues including integrity, fairness, transparency and general market stability and many of these issues were fiercely contested. Thus while one source has described the betting exchanges as “The bastard child of a disruptive technology” (Bettingmarket.com 2005) the Joint Committee on the Draft Gambling Bill (United Kingdom Parliament 2004) has argued that “there is nothing inherently perverse about the fundamental concept of betting exchanges” and it recognised that the betting exchanges offer “a shrewd business model”. The aim here is not to provide full chapter and verse on the legislation that has emerged but rather to contrast the approaches to the regulation of the betting exchanges adopted by the betting shop chains and the betting exchange companies.

In 2004 the UK based betting exchanges established a voluntary code of practice designed to provide a self-regulatory framework for the operation of betting exchanges. The first of its provisions sought to preserve the integrity of sporting events and looked to enshrine a number of principles including a commitment to work constructively and to share information with, and to give assistance in any investigation or disciplinary inquiry to appropriate sporting regulators and to ensure that all customers consented to the release of their data to the sporting regulator. For their part the traditional large betting shop companies have stressed that the betting exchanges threaten the integrity of sport. The betting shop companies suggested that there are two activities, which threaten the integrity of betting on the exchanges namely, what is in effect, insider trading and the artificial manipulation of prices.

The principal argument here was that because the exchanges offer customers the opportunity to bet that a horse, for example, would lose a race, this created opportunities for fixing races in that jockeys, owners and others may lay their horse to lose. The fear was expressed that those with such ‘inside information’ would be able to make a profit from a uninformed customer and to compromise the integrity of horse racing or any other sporting event. These continuing fears have been fuelled in recent years by a number of suspicious betting patterns on horse races and in darts and snooker competitions within the UK. The betting exchange companies have been keen to refute allegations that they are undermining the integrity of horse racing or of any other sport. Indeed two betting exchange companies, Betfair and Sporting Options stress that they signed a Memorandum of Understanding with the Jockey Club, one of the three governing bodies in horse racing and the one responsible for regulating the conduct of horseracing in Great Britain, which allows it access to betting information on horse races where betting patterns arouse suspicion or concern. More pointedly the exchange companies have called for a new code of practice for betting shops to bring them into line with the standards of probity and openness that they themselves have set.

Fairness has attracted considerable attention and here the debate has focused on two principal issues namely the licensing of customers who lay prices on the exchanges and the question of taxation and the levy. The betting shop companies argued that customers using the exchanges to lay bets, and thus effectively operating as, and falling within the definition of, bookmakers, should be subject to the same fiscal and regulatory regime as bookmakers. The betting exchange companies for their part argued that it is unnecessary for their customers to be licensed because the licence conditions for the exchanges themselves are sufficient to ensure that regulatory aims could be achieved without the additional administrative burden of regulating individual customers.

The betting shop companies have expressed concern about what they described as the differential in tax and levy paid by the betting exchange customers who lay horses on the one hand and traditional bookmakers on the other. One of the arguments here, for example, is that the betting shop

companies are not competing on equal terms. While the betting exchange companies pay tax on the commission they charge, those customers who lay bets do not pay tax whereas bookmakers who lay bets have to pay the Gross Profits Tax first introduced by the Government for the betting industry in 2001. Similar arguments have been made about the betting exchanges contribution to the levy which is not calculated on the commission for bets struck on the exchanges but on the companies' winnings on bets struck in the betting shops. The betting exchange companies argued that as there is no betting tax on individual customers within the UK there was no case to tax their customers because they chose to bet on the exchanges rather than in betting shops.

The major betting shop and betting exchange players have been the major contributors to the debates about taxation and the levy but some wider issues have also emerged. On the one hand, for example, as a number of traditional large on-course bookmakers, some bookmakers based overseas and growing numbers of high staking customers trade on the exchanges so the fiscal position may change and lead to significant reductions in tax and levy revenues so the demands for greater regulation may build. On the other hand any substantial, and potentially more punitive, changes to the current taxation and levy position could effectively serve to force the leading betting exchange companies to base their operation overseas thus not only putting them outside the UK's regulatory, taxation and levy regime whilst also weakening the UK's role as a major centre within the competitive global betting market.

The issues of privacy, transparency, versatility and the general stability of the betting market have also played a part in the debates concerning regulation but they have featured much less prominently. The betting exchanges claim to guarantee privacy for their customers in that they do not permit customers to identify themselves to each other either through personal contact or otherwise. Betting shop customers do not enjoy as much privacy in that as visitors to prominent high street outlets they are visible to other customers and will on occasion be seen by work colleagues, family members or friends. However the betting shop companies have argued that the anonymity afforded to betting exchange customers offers an opportunity for customers with 'inside information' to get friends and associates to bet, and particularly to lay bets, for them thereby effectively nullifying the exchanges commitment to release information to sporting regulators. The betting exchange companies argued they offer transparency and versatility, which they claimed produces a fair market, in that all customers are provided with access to the same market information, in that they can change their betting actions before and during events and in that their prices are significantly better than those on offer within the betting shops. Finally the debate about the general stability of the betting market centred not only around the threat the betting exchanges are seen to pose to the traditional betting industry and more particularly to its traditional major players the betting shop companies but also on the fact that one company currently dominates the exchange market and that this might deter new entrants and hence stifle competition within that market.

Discussion

The emergence of the betting exchanges has begun to transform the traditional sports betting market and the debate about their regulation provides valuable perspectives on the regulatory positions adopted by the two sets of key players. At the same time it also offers some insights into the debates about public interest versus private interest regulation, into how stakeholders shape regulatory practices and frameworks and into the relationships between the state and capital and on theorisations of the role and functions of the state within capitalist societies. Both public and private interests can be identified as important drivers in these debates. Public interests are reflected, for example, in the desire to ensure that gambling is conducted in a fair and open way, in that that arrangements should be in place to seek to maintain the public's confidence in the integrity of sporting events, in concerns about reductions in the taxation revenues paid into the public purse and in the desire to ensure that all customers are treated equally whether they place their bets in the betting shops or on the betting exchanges. Private interests, on the other hand, are seen to be reflected, for example, in the desire to protect the respective commercial interests of the betting shop

and betting exchange companies and especially in the claims made for the need to protect the levy paid to maintain and enhance the UK's horse racing industry.

While both the major players in the debate have sought to stress that their proposals for regulation are, in their different ways, in the public interest, there is little explicit evidence of them inviting the public per se to contribute to this debate or of any attempt to systematically canvas public opinion in making their case for regulatory procedures. That said the rapid growth of betting taking place on the exchanges might, in part at least, be seen to be evidence that as customers vote with their feet, or perhaps more accurately in this case, with their fingers, so what the betting shop companies see as lax regulation are in tune with opinion. At the same time the boundaries between public interests, on the one hand, and private interests on the other are in some ways blurred. Thus while the rapid growth of the betting exchanges may pose a threat to the viability of many betting shops and thus prove damaging to the major betting shop companies this may also lead to job losses for the public at large. In a similar vein while the UK's horse racing industry is dominated by some wealthy players it also provides work for many ordinary people and any threat to the industry threatens their employment.

The debate about the regulation of betting exchanges also sheds some light on the relationship between the state and retail capital and on the theorisations of the role and the functions of the state within capitalist societies. The general drift of the debate within the current case study suggests regulation generally favours the betting exchanges rather than the betting shops and this in turn suggests the privileging of new capital interests over traditional capital interests. This is not wholly consistent with other research findings, which indicate the dominance of corporate retail capital over smaller capital factions (Wrigley and Lowe, 2002; Jones, Comfort and Hillier, 2004). At the same time the importance attached to public interest in the debates about the regulation of the betting exchanges suggests that theorisations of the state grounded exclusively in economics tell only a partial story. More generally the move to what the established betting shop companies view as a more relaxed regulatory approach to the betting exchanges may also be seen to reflect the challenges associated not only with new virtual ICT technologies but also the forces of globalisation. While the state wants to regulate the exchanges as part of its wider approach to gambling it also recognises the need to ensure that the regulatory regime it imposes does not stifle development or drive the UK based betting exchanges overseas where they will not only be beyond the UK's regulatory jurisdiction but also where they will be lost to the UK economy and weaken its role on the competitive global betting market.

Conclusion

The betting exchanges have brought a new business model and innovative dimensions to sports betting within the UK. This simple case study provides an exploratory examination of the debate surrounding the regulation of betting exchanges. The debate embraced a range of inter-related issues but was focused particularly on the integrity of sporting events and fairness and it offered some perspectives not only on the regulatory positions adopted by the two principal players, namely the betting shop companies and the betting exchange companies who are respectively for running of the old and the new sports betting models but also on the relationship between private and public sector interests within the regulatory process. The case study also provides some specific empirical illustrations of the challenges involved in regulating new developments in Information and Communication Technologies and some insights into the relationship between the state and retail capital and on the theorisations of the role of the state within modern capitalist societies.

References

1. Bettingmarket.com (2005) 'Betting Exchanges', <http://www.bettingmarket.com/bettingexchanges.htm>
2. Cranor, L.F. and Wildman, S.S. (2002) 'Rethinking Rights and Regulations', MIT Press, Cambridge.
3. Crewe, L. (2000) 'Geographies of retailing and consumption', *Progress in Human Geography* 24, pp. 275-290.

4. Jones, P., Comfort, D. and Hillier, D. (2004) 'The Regulation of Street Trading in the UK', *Geography*, 89, 3, pp. 248-253.
5. Lowe, M. and Wrigley, N. (1996) 'Towards the new retail geography' in Wrigley N. and Lowe M. eds *Retailing, Consumption and Capital* Longman, London 3-30.
6. Mintel (2005a) 'Betting Shops UK-July 2005', Mintel, London.
7. Mintel (2005b) 'Remote Betting-UK-August 2005', Mintel, London.
8. Newman, A.J. and Cullen, P. (2002) 'Retailing: Environment and Operations', Thomson, London.
9. Pierson, C. (1996) 'The Modern State', Routledge, London.
10. Racing Economics (2003) 'The changing future of the British Horse Racing sector to 2010', http://www.racingeconomics.com/racing_future_prospectus.pdf
11. Research and Markets (2004) 'Betting Exchanges – The eBay of the Betting Industry', <http://www.researchandmarkets.com/reports/296019/296019.htm>
12. Strange, S. (1996) 'The retreat of the state: The diffusion of power in the world economy', Cambridge University Press, Cambridge.
13. Svantesson, D.J.B. (2005) 'The characteristics making Internet communication challenge traditional models of regulation – What every international jurist should know about the Internet', *International Journal of Law and Information Technology*, 13, 1, pp. 39-69.
14. The United Kingdom Parliament (2004) Joint Committee on the Draft Gambling Bill-First Report, <http://www.parliament.the-stationery-office.co.uk/pa/jt200304/jtselect/jtgamb/63/6302.htm>
15. Wrigley, N. and Lowe, M. (2002) 'Reading Retail's' Arnold London.