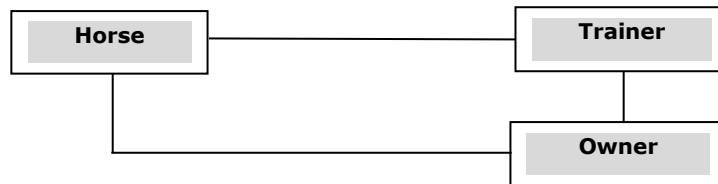

THE DIFFERENCE BETWEEN THE MOST COMMON FORMS OF RACEHORSE OWNERSHIP

1. OVERVIEW

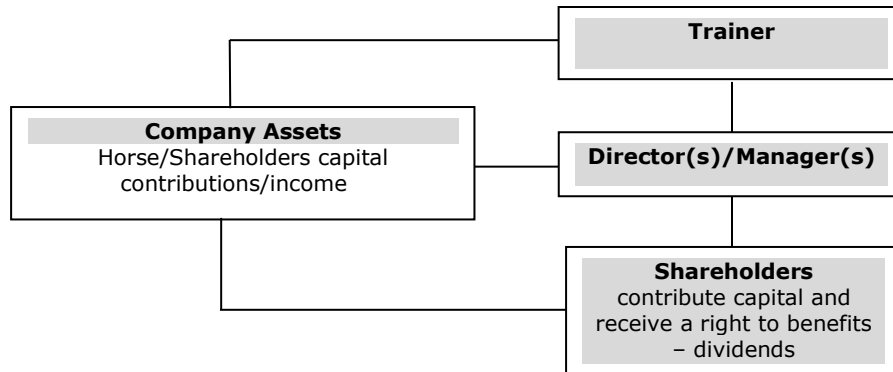
- 1.1 Owning thoroughbred racehorses can be highly enjoyable and rewarding, particularly if you are lucky enough to own a horse that progresses to winning races, and if your horse is a fashionably bred colt and just happens to win a Group 1 race, then a stud deal is likely to be available.
- 1.2 But it is also highly speculative, as Owners are required to incur significant liabilities and expense without the assurance of any financial return.
- 1.3 Significant risks associated with the ownership of thoroughbred racehorses include that the horse may die, or value is diminished because of the materialisation of an inherent risk, including accident, illness, infertility or sub-fertility, injury, or natural cause, or simply not progress to competing in or winning any races or Prize money.
- 1.4 Insurance cover is available against some, but not all, of those risks.
- 1.5 Furthermore, it should be appreciated that most colts are gelded for behavioural and physical reasons.
- 1.6 A person may elect to race a horse as a sole owner or with other like-minded people.
- 1.7 The most common forms of legal ownership of a racehorse are:
 - (a) Sole Ownership:
 - (i) Individual; or
 - (ii) Corporate entity; and
 - (b) Multiple Party Ownership Arrangements:
 - (i) Co-ownership;
 - (ii) Partnership; or
 - (iii) Trust.
- 1.8 The form you choose will determine or influence, amongst other things:
 - (a) the nature of your entitlement to benefits (including prize money) and liability for obligations (including payment of ongoing fees and expenses);
 - (b) how you go about insuring your investment against various insurable risks;
 - (c) your liability to pay income and capital gains tax; and
 - (d) your capacity to sell your interest (in the horse) if you wish to do.
- 1.9 Before deciding on your preferred form of legal ownership, you should ensure that you know the differences between them and how those differences may affect you.

2. Sole ownership – Individual



Sole Ownership is the simplest legal form of racehorse ownership. The Owner (individual or corporate entity) owns the whole of the horse, is entitled to receive the whole of any prize money earned by the horse and is solely responsible for the trading of the sole enterprise.

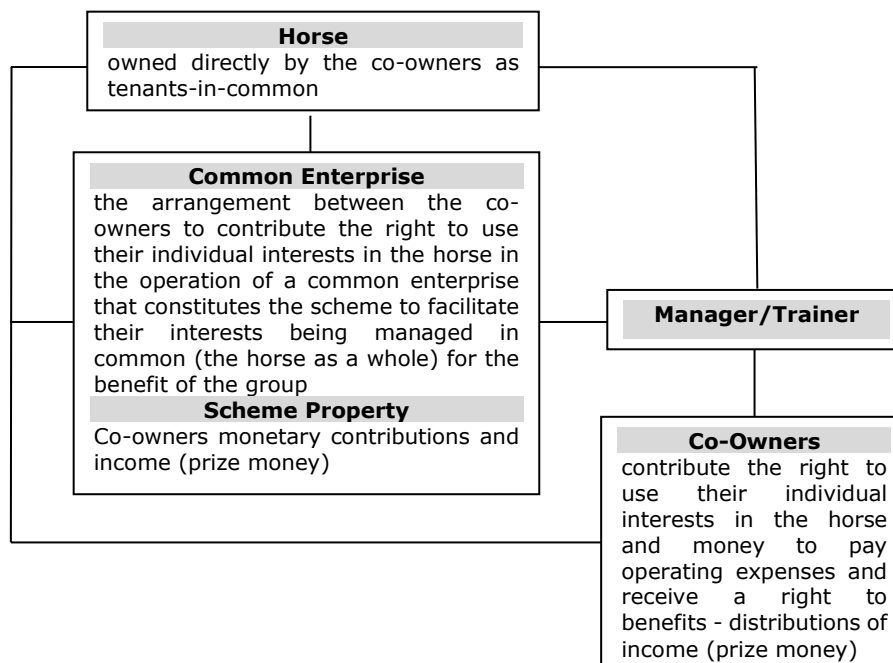
3. Sole Ownership – Corporate Entity



The most common form of corporate entity in Australia is the Pty Ltd (privately held) Company. It can have up to 50 non-employee shareholders and must have at least 1 director who is an Australian resident. The directors are responsible for the operation and trading of the company, including (without limitation) an obligation to ensure the company is liquid and solvent. The liability of its shareholders to pay the debts of the company is limited to the share capital of the company.

Significantly, the legal and equitable title to the horse is held by the company for the benefit of its shareholders and is a company asset.

4. Co-ownership



- 4.1 Co-ownership is the most common legal form of racehorse ownership involving 2 or more people owning a thoroughbred horse for the purpose of using it for racing. It is considered the most flexible and accommodating of the varying and often changing needs of the individual members.
- 4.2 Such schemes are typically contract-based “common enterprise” arrangements, with the ownership of the horse divided into proportionate ownership interests owned by no more than 20 members in the normal course, with up to 50 members permitted under the ASIC Instrument [in the case of shares being offered by a licensed promoter under a lead regulator approved Product Disclosure Statement], as “tenants-in-common”, subject to the terms of the co-owners agreement or deed.
- 4.3 The realities of horse racing schemes that are **co-ownership** contract-based “**common enterprise**” arrangements, as they are designed to operate in practice, are:
- (1) People contribute money to acquire from the promoter/operator (or other holder of an ownership interest) proportionate ownership interests in a thoroughbred horse, as tenants-in-common, for the purpose of using it for racing on the basis that they will:
 - (a) assume various obligations, including to contribute:
 - (i) the right to use their individual ownership interests in the horse in a common enterprise (scheme) to enable the ownership interests of all tenants-in-common comprising the horse “as a whole” to be managed by a person as the “operator” of the scheme on behalf of the group; and
 - (ii) money (on an ongoing basis) towards the scheme’s operating expenses, in the same proportions as the ownership interests held [Clauses 3.3, 7.1 and 7.2 of **TOR COA**];

as consideration to acquire rights (interests) to benefits produced by the scheme; and
 - (b) acquire rights (interests) to benefits produced by the scheme, including to:
 - (i) participate as members of the scheme for the purpose of using the horse “as a whole” for racing with the objective of earning income for the benefit of the group [benefits derived as the holders of rights or interests in property]; and
 - (ii) receive any income (net prize money) earned, in the same proportions as the ownership interests held [a financial benefit produced by the scheme. [Clause 3.2 of **TOR COA**].
 - (2) The contributions by all tenants-in-common of the right to use their individual ownership interests to be used in the scheme’s operations, and the legally binding contractual promise to contribute money (on an ongoing basis) towards the scheme’s operating expenses, in the same proportions as the ownership interests held, as consideration to acquire rights (interests) to benefits produced by the scheme, while not money, are of **money’s worth**, and a “fair equivalent” of what is received.
 - (3) Each member’s ownership interest in the property of the group [the horse “as a whole”] which is the subject of the scheme’s operations, (not the scheme itself so far as that is different), from an operational perspective, is inseparable from the ownership interests of the other members and the horse “as a whole, and incapable of being separately managed.
 - (4) The right of the members to separately manage their individual ownership interests is:
 - (a) subordinated to the rights of the members collectively and the authority of the manager and the trainer [with actual possession and control of the horse “as a whole”] to operate the scheme on behalf of the group; and
 - (b) limited to voting on those matters specified in the relevant Owners Agreement or Training Agreement as requiring the members’ approval (by the requisite majority).
 - (5) The manager and the trainer are both clearly “operators” of the scheme who:
 - (a) control aspects of the scheme’s operations on behalf of the members collectively;
 - (b) manage “as a whole” the property of the group [the members’ individual interests in common - the horse “as a whole”]; and

- (c) procure the services of other service providers such as veterinarians, farriers, jockeys, gisters and pre-trainers, etc.

Neither of them is a mere “agent” who separately manages the property of each member or “investment professional” who simply provides advice to the members on enhancing the value of their own property without exercising control.

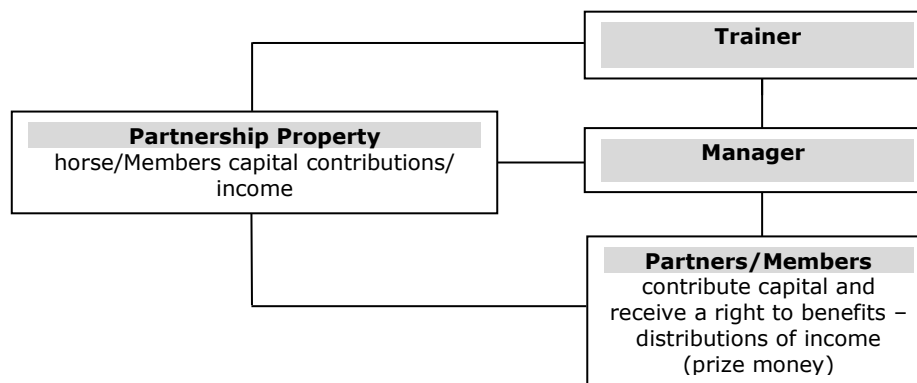
- 4.4 In other words, day-to-day control over the operation of the scheme devolves to the manager and the trainer, being the people who, as the operators of the scheme, actually perform “...*the acts which constitute the management of or the carrying out of the activities which constitute the scheme*”.
- 4.5 Co-owners are usually “**severally**” liable for a proportion of the scheme’s operating expenses, in the same proportions as the interests held. This means that if a Co-owner breaches a payment obligation, a creditor has the right to proceed against only the defaulting co-owner for recovery of the full amount of the defaulting co-owner’s outstanding payment obligations.
- 4.6 Co-owners should be aware that:
 - (a) they are members of a legal binding common enterprise arrangement comprising all the co-owners;
 - (b) the common enterprise must be **liquid** and **solvent** to be able to operate; and
 - (c) a breach by any co-owner of payment obligations may result in:
 - (i) the common enterprise being **illiquid** or **insolvent** and therefore unable to operate; and
 - (ii) the trainer stopping or suspending training of the horse (as a whole) until all outstanding accounts of the trainer and third-party service providers procured by the trainer to provide services in relation to the horse are fully paid.
- 4.7 The common enterprise will be:
 - (a) **liquid** if it has available funds to pay all operating costs when due; and
 - (b) **solvent** if all the Co-owners are able and willing to pay their respective proportions of operating costs, either:
 - (i) directly to the trainer and other third-party service providers (if proportionate direct invoicing has been agreed to); or
 - (ii) as contributions to a designated bank account maintained by the Manager, when due.
- 4.8 Conversely, the common enterprise will be:
 - (a) **illiquid** if it does not have liquid funds to pay such costs when due; and
 - (b) **insolvent** if any of the current co-owners are unable or unwilling to pay their respective proportions of such costs when due].
- 4.9 A co-ownership arrangement should be the subject of a comprehensive governing legal document. Such a document promotes and supports the efficient operation of the common enterprise, and reduces the risk of agency problems, such as conflicts between:
 - (a) co-owners;
 - (b) co-owners and the manager; and
 - (c) the other constituencies of the common enterprise, including the trainer and other third-party service providers and creditors.
- 4.10 Without a written agreement setting out how important decisions relating to the operation of the common enterprise are to be made, it is often difficult for the co-owners to make those decisions, including deciding:
 - (a) who should manage and operate the common enterprise on behalf of the co-owners;

- (b) who should train the horse and whether there should be a change of trainer;
- (c) whether the horse, if it is a colt, should be gelded;
- (d) what action should be taken by the manager (on behalf of the other co-owners) to ensure that:
 - (i) any breach by a co-owner of a payment obligation is remedied; and
 - (ii) the common enterprise is **liquid** and **solvent**;
- (e) if the horse, or an interest in the horse, should be sold;
- (f) if the horse should be retired from racing; and
- (g) if the common enterprise should be wound up because its purpose either has been accomplished or cannot be accomplished [including if it is **illiquid** or **insolvent**].

4.11 It will always be easier for the parties to agree the key elements of their co-ownership arrangement at the beginning, when expectations and level of goodwill between the parties are high, rather than later when their attitudes and circumstances may have changed.

4.12 If the co-owners do not expressly agree to their own terms and set them out in an Owners Deed or agreement, then the terms of the **TOR Co-owners Agreement (TOR COA)** will be deemed to apply under the **Australian Rules of Racing (ARR)**.

5. Partnership



5.1 A partnership is:

- (a) an arrangement between 2 or more people (members), not exceeding 20, with a view to profit;
- (b) a single unincorporated legal entity.

5.2 In the case of a scheme that is a typical partnership arrangement the members agree to:

- (a) participate as a member of the scheme established for the purpose of acquiring a thoroughbred horse for the purpose of using it for racing;
- (b) contribute money to or on behalf of the scheme to facilitate their pooled funds being used to:
 - (i) acquire the horse as a whole for use as the property of the scheme and the benefit of the members as a group; and
 - (ii) pay operating expenses, including horse expenses;
- (c) apportion the benefits, including owners' raceday ticketing and the right of the members to receive distributions of income;
- (d) appoint a manager and a licensed trainer [with actual possession of the horse as a whole] and delegate to them the authority to operate aspects of the scheme on behalf of the members as a group; and

(e) hold their individual interests in the scheme, including the horse as a whole as partnership property, subject to the terms of the partnership deed or agreement.

5.3 The right of the members to control over their individual interests in the scheme, including the horse as a whole, is effectively:

(a) subordinated to the rights of the members as a group and the authority of the manager and the trainer [with actual possession of the horse as a whole] to operate the scheme on behalf of the group; and

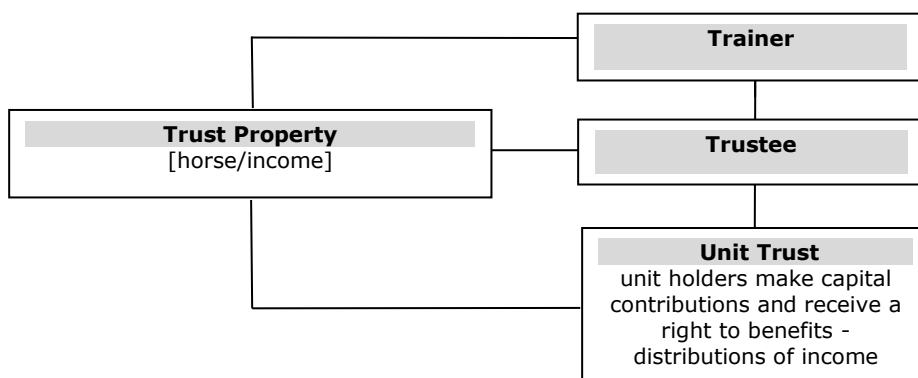
(b) limited to voting on those matters specified in the relevant Partnership Agreement or Training Agreement as requiring the members' approval (by the requisite majority).

5.4 The rights and obligations of the members will be governed by the applicable Partnership Agreement which should be in writing. It will also be subject to the provisions of the Partnership Act of the relevant state or territory.

5.5 Unlike companies and co-ownership arrangements, partnerships have unlimited liability [except for limited liability partnerships, which are rare]. The members may set limits on how much each of them will be required to contribute to the partnership, but legally, each participating member's liability to creditors is unlimited. This means that all members are collectively responsible [**jointly and severally** liable] for all business debts and for ensuring that the partnership is **liquid** and **solvent**.

5.6 Any member (regardless of the interest held) may also have a statutory right to terminate the partnership, requiring the sale of the horse and partitioning of the sale proceeds.

6. Trust



6.1 A trust structure can be employed in a business or for trading purposes. A trust involves the trustee (usually either an individual or corporate entity) holding the legal title to the trust property in the name of the trust for the benefit of the unitholders or beneficiaries of the trust.

6.2 A trust itself does not pay income tax on profits, provided that the profits of the trust have been fully distributed to the beneficiaries in the relevant financial year.

6.3 The two main types of trusts are:

(a) unit trusts; and

(b) discretionary trusts.

6.4 In a typical unit trust, beneficiaries' hold units in the trust, and the trustee distributes the income to the unitholders in accordance with their unitholding [in the same proportions as the number of units held by each unitholder bears to the total number of units issued].

6.5 Like a shareholder in a company, a unitholder in a unit trust has a specific entitlement to a proportion of the income or property of the trust [in the same proportions as the number of units held].

6.6 On the other hand, in a discretionary trust, the trustee typically has the discretion to decide which beneficiaries will receive distributions of both income and capital, and what amounts, if any, they will receive between them. This discretion as to the distribution of income and capital, which should be exercised afresh each financial year, is a significant advantage in tax planning. Subject to the

Corporations Act 2001 (Cth), limited liability may also be achieved with discretionary trusts by using a corporate trustee. Discretionary trusts are a common choice for family-run businesses.

This article was compiled by
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Tony Fleiter specializes in acting for participants in the thoroughbred horse industry. His clients include some of Australia’s leading breeders, owners, studmasters and trainers.

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