

# CHURCHILL DOWNS INC

## FORM 10-Q (Quarterly Report)

Filed 11/03/10 for the Period Ending 09/30/10

|             |  |
|-------------|--|
| Address     | 700 CENTRAL AVE<br>LOUISVILLE, KY 40208  |
| Telephone   | 5026364400                               |
| CIK         | 0000020212                               |
| Symbol      | CHDN                                     |
| SIC Code    | 7948 - Racing, Including Track Operation |
| Industry    | Casinos & Gaming                         |
| Sector      | Services                                 |
| Fiscal Year | 12/31                                    |

UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION  
WASHINGTON, D.C. 20549

FORM 10-Q

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended September 30, 2010

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission file number 001-33998



CHURCHILL DOWNS  
INCORPORATED

(Exact name of registrant as specified in its charter)

**Kentucky**

(State or other jurisdiction of incorporation or organization)

**61-0156015**

(IRS Employer Identification No.)

**700 Central Avenue, Louisville, Kentucky 40208**

(Address of principal executive offices) (zip code)

**(502) 636-4400**

(Registrant's telephone number, including area code)

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports) and (2) has been subject to such filing requirements for the past 90 days. Yes  No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

Indicate by check mark whether the Registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

Large accelerated filer

Non-accelerated filer

Accelerated filer

Smaller reporting company

Indicate by check mark whether the Registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes  No

The number of shares outstanding of registrant's common stock at October 28, 2010 was 16,577,599 shares.

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**Table of Contents**

**CHURCHILL DOWNS INCORPORATED  
INDEX TO QUARTERLY REPORT ON FORM 10-Q  
For the Quarter Ended September 30, 2010**

**Part I-FINANCIAL INFORMATION**

|         |  |    |
|---------|--|----|
| Item 1. | Financial Statements   |    |
|         | Condensed Consolidated Balance Sheets, September 30, 2010 and December 31, 2009 (Unaudited)  | 3  |
|         | Condensed Consolidated Statements of Net (Loss) Earnings for the three and nine months ended September 30, 2010 and 2009 (Unaudited) | 4  |
|         | Condensed Consolidated Statements of Cash Flows for the nine months ended September 30, 2010 and 2009 (Unaudited)                    | 5  |
|         | Notes to Condensed Consolidated Financial Statements (Unaudited)   | 7  |
| Item 2. | Management’s Discussion and Analysis of Financial Condition and Results of Operations  | 20 |
| Item 3. | Quantitative and Qualitative Disclosures About Market Risk   | 40 |
| Item 4. | Controls and Procedures  | 40 |

**Part II-OTHER INFORMATION**

|          |   |    |
|----------|---|----|
| Item 1.  | Legal Proceedings   | 40 |
| Item 1A. | Risk Factors  | 42 |
| Item 2.  | Unregistered Sales of Equity Securities and Use of Proceeds | 43 |
| Item 3.  | Defaults Upon Senior Securities (Not applicable)            | 43 |
| Item 4.  | Removed and Reserved  | 43 |
| Item 5.  | Other Information (Not applicable)                          | 43 |
| Item 6.  | Exhibits  | 43 |
|          | Signatures  | 44 |
|          | Exhibit Index   | 45 |

## Table of Contents

### PART I. FINANCIAL INFORMATION

#### ITEM 1. FINANCIAL STATEMENTS

##### CHURCHILL DOWNS INCORPORATED CONDENSED CONSOLIDATED BALANCE SHEETS (Unaudited) (in thousands)

|  | September 30,     | December 31,      |
|--|-------------------|-------------------|
|  | 2010              | 2009              |
| <b>ASSETS</b>  |                   |                   |
| Current assets:  |                   |                   |
| Cash and cash equivalents  | \$ 14,533         | \$ 13,643         |
| Restricted cash  | 61,101            | 35,125            |
| Accounts receivable, net of allowance for doubtful accounts of \$3,195 in 2010 and \$1,024 in 2009                                       | 22,472            | 33,446            |
| Deferred income taxes  | 8,231             | 6,408             |
| Other current assets   | 19,555            | 16,003            |
| Total current assets   | 125,892           | 104,625           |
| Property and equipment, net  | 465,922           | 458,222           |
| Goodwill   | 183,394           | 115,349           |
| Deferred income taxes  | 5,373             | —                 |
| Other intangible assets, net   | 56,842            | 34,329            |
| Other assets   | 12,508            | 12,877            |
| Total assets   | <u>\$ 849,931</u> | <u>\$ 725,402</u> |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>  |                   |                   |
| Current liabilities:   |                   |                   |
| Accounts payable   | \$ 38,149         | \$ 35,034         |
| Bank overdraft   | 10,667            | 3,738             |
| Purses payable   | 16,223            | 11,857            |
| Accrued expenses   | 52,384            | 46,603            |
| Liabilities associated with assets held for dissolution  | 1,089             | —                 |
| Dividends payable  | —                 | 6,777             |
| Deferred revenue   | 17,597            | 30,972            |
| Income taxes payable   | 501               | 1,997             |
| Deferred riverboat subsidy   | 38,613            | 23,965            |
| Note payable, related party  | —                 | 24,043            |
| Total current liabilities  | 175,223           | 184,986           |
| Long-term debt   | 109,500           | 71,132            |
| Convertible note payable, related party  | 14,970            | 14,655            |
| Other liabilities  | 20,147            | 19,137            |
| Deferred revenue   | 15,532            | 16,720            |
| Deferred income taxes  | —                 | 11,750            |
| Total liabilities  | 335,372           | 318,380           |
| Commitments and contingencies  |                   |                   |
| Shareholders' equity:  |                   |                   |
| Preferred stock, no par value; 250 shares authorized; no shares issued   | —                 | —                 |
| Common stock, no par value; 50,000 shares authorized; 16,577 shares issued September 30, 2010 and 13,684 shares issued December 31, 2009 | 234,712           | 145,423           |
| Retained earnings  | 279,847           | 261,599           |
| Total shareholders' equity   | 514,559           | 407,022           |
| Total liabilities and shareholders' equity   | <u>\$ 849,931</u> | <u>\$ 725,402</u> |

The accompanying notes are an integral part of the condensed consolidated financial statements.

**Table of Contents**

**CHURCHILL DOWNS INCORPORATED**  
**CONDENSED CONSOLIDATED STATEMENTS OF NET (LOSS) EARNINGS**  
**for the three and nine months ended September 30,**  
**(Unaudited)**  
**(in thousands, except per common share data)**

|   | <u>Three Months Ended</u><br><u>September 30,</u> |                   | <u>Nine Months Ended</u><br><u>September 30,</u> |                  |
|---|---|-------------------|--|------------------|
|   | <u>2010</u>                                       | <u>2009</u>       | <u>2010</u>                                      | <u>2009</u>      |
| Net revenues  | \$135,744   | \$100,896         | \$411,306  | \$354,670        |
| Operating expenses  | 117,168   | 85,344            | 331,533  | 272,556          |
| Selling, general and administrative expenses                          | 15,281  | 13,092            | 43,937   | 37,527           |
| Operating income  | 3,295   | 2,460             | 35,836   | 44,587           |
| Other income (expense):   |   |                   |  |                  |
| Interest income   | 30  | 393               | 158  | 780              |
| Interest expense  | (1,625)   | (245)             | (4,303)  | (772)            |
| Equity in loss of unconsolidated investments                          | (470)   | (568)             | (317)  | (641)            |
| Miscellaneous, net  | 1,832   | 322               | 2,485  | 1,042            |
|   | <u>(233)</u>                                      | <u>(98)</u>       | <u>(1,977)</u>                                   | <u>409</u>       |
| Earnings from continuing operations before provision for income taxes | 3,062   | 2,362             | 33,859   | 44,996           |
| Income tax benefit (provision)  | 638   | (3,578)           | (10,034)   | (20,423)         |
| Earnings (loss) from continuing operations                            | 3,700   | (1,216)           | 23,825   | 24,573           |
| Discontinued operations, net of income taxes:                         |   |                   |  |                  |
| Loss from operations  | (4,389)   | (1,109)           | (5,577)  | (863)            |
| Net (loss) earnings   | <u>\$ (689)</u>                                   | <u>\$ (2,325)</u> | <u>\$ 18,248</u>                                 | <u>\$ 23,710</u> |
| Net (loss) earnings per common share data:                            |   |                   |  |                  |
| Basic   |   |                   |  |                  |
| Earnings (loss) from continuing operations                            | \$ 0.22   | \$ (0.09)         | \$ 1.56  | \$ 1.75          |
| Discontinued operations   | (0.26)  | (0.08)            | (0.36)   | (0.06)           |
| Net earnings (loss)   | <u>\$ (0.04)</u>                                  | <u>\$ (0.17)</u>  | <u>\$ 1.20</u>                                   | <u>\$ 1.69</u>   |
| Diluted   |   |                   |  |                  |
| Earnings (loss) from continuing operations                            | \$ 0.22   | \$ (0.09)         | \$ 1.56  | \$ 1.75          |
| Discontinued operations   | (0.26)  | (0.08)            | (0.36)   | (0.06)           |
| Net earnings (loss)   | <u>\$ (0.04)</u>                                  | <u>\$ (0.17)</u>  | <u>\$ 1.20</u>                                   | <u>\$ 1.69</u>   |
| Weighted average shares outstanding                                   |   |                   |  |                  |
| Basic   | 16,311  | 13,587            | 14,796   | 13,578           |
| Diluted   | 16,768  | 13,587            | 15,257   | 14,040           |

The accompanying notes are an integral part of the condensed consolidated financial statements.

**Table of Contents**

**CHURCHILL DOWNS INCORPORATED**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**for the nine months ended September 30,**  
**(Unaudited) (in thousands)**

|   | <u>2010</u>      | <u>2009</u>      |
|---|------------------|------------------|
| <b>Cash flows from operating activities:</b>  |                  |                  |
| Net earnings  | \$ 18,248        | \$ 23,710        |
| Adjustments to reconcile net earnings to net cash provided by operating activities:                                   |                  |                  |
| Depreciation and amortization   | 34,410           | 22,399           |
| Asset impairment loss   | 1,598            | —                |
| Equity in loss of unconsolidated investments  | 317              | 641              |
| Unrealized gain on derivative instruments   | (612)            | (612)            |
| Share-based compensation  | 2,388            | 2,338            |
| Other   | 1,192            | 458              |
| Increase (decrease) in cash resulting from changes in operating assets and liabilities, net of business acquisitions: |                  |                  |
| Restricted cash   | (20,395)         | (22)             |
| Accounts receivable   | 2,099            | (2,657)          |
| Other current assets  | (1,549)          | (394)            |
| Accounts payable  | (6,656)          | (6,231)          |
| Purses payable  | 4,367            | 4,172            |
| Accrued expenses  | 7,250            | 4,848            |
| Deferred revenue  | 11,423           | (3,253)          |
| Income taxes payable  | (554)            | 23,273           |
| Other assets and liabilities  | 1,815            | (5,801)          |
| Net cash provided by operating activities   | <u>55,341</u>    | <u>62,869</u>    |
| <b>Cash flows from investing activities:</b>  |                  |                  |
| Additions to property and equipment   | (56,493)         | (32,305)         |
| Contingency payment for acquisition of business   | —                | (3,500)          |
| Acquisition of business, net of cash acquired   | (32,408)         | —                |
| Purchases of minority investments   | (400)            | (1,894)          |
| Acquisition of gaming license   | (2,750)          | (3,250)          |
| Proceeds on sale of property and equipment  | 16               | 8                |
| Change in deposit wagering asset  | (37)             | 307              |
| Net cash used in investing activities   | <u>(92,072)</u>  | <u>(40,634)</u>  |
| <b>Cash flows from financing activities:</b>  |                  |                  |
| Borrowings on bank line of credit   | 204,260          | 253,314          |
| Repayments on bank line of credit   | (141,849)        | (263,454)        |
| Repayment of note payable, related party  | (24,043)         | —                |
| Change in book overdraft  | 6,929            | (2,041)          |
| Payment of dividends  | (6,777)          | (6,767)          |
| Repurchase of common stock  | (1,354)          | (89)             |
| Common stock issued   | 459              | 427              |
| Change in deposit wagering liability  | (4)              | 269              |
| Net cash provided by (used in) financing activities   | <u>37,621</u>    | <u>(18,341)</u>  |
| Net increase in cash and cash equivalents   | 890              | 3,894            |
| Cash and cash equivalents, beginning of period  | 13,643           | 12,658           |
| Cash and cash equivalents, end of period  | <u>\$ 14,533</u> | <u>\$ 16,552</u> |

The accompanying notes are an integral part of the condensed consolidated financial statements.

**CHURCHILL DOWNS INCORPORATED**  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**for the nine months ended September 30,**  
**(Unaudited) (in thousands)**

|   | <u>2010</u> | <u>2009</u> |
|---|-------------|-------------|
| <b>Supplemental disclosures of cash flow information:</b>                   |             |             |
| Cash paid during the period for:  |             |             |
| Interest  | \$ 2,706    | \$ 302      |
| Income taxes  | \$ 7,014    | \$6,829     |
| <b>Schedule of non-cash investing and financing activities:</b>             |             |             |
| Issuance of common stock in connection with acquisition of business         | \$86,497    | \$ —        |
| Issuance of common stock in connection with LTIP and restricted stock plans | \$ 2,525    | \$ —        |

The accompanying notes are an integral part of the condensed consolidated financial statements.

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
**(Unaudited)**

**NOTE 1 — BASIS OF PRESENTATION**

The accompanying Condensed Consolidated Financial Statements are presented in accordance with the requirements of this Quarterly Report on Form 10-Q and consequently do not include all of the disclosures required by accounting principles generally accepted in the United States of America or those normally made in Churchill Downs Incorporated's (the "Company") Annual Report on Form 10-K. The year-end Condensed Consolidated Balance Sheet data was derived from audited financial statements but does not include all disclosures required by accounting principles generally accepted in the United States of America. Accordingly, the reader of this Quarterly Report on Form 10-Q should refer to the Company's Annual Report on Form 10-K for the year ended December 31, 2009 for further information. The accompanying Condensed Consolidated Financial Statements have been prepared in accordance with the Company's customary accounting practices and have not been audited.

In the opinion of management, all adjustments necessary for a fair statement of this information have been made, and all such adjustments are of a normal, recurring nature.

The Company's revenues and earnings are significantly influenced by its racing calendar. Therefore, revenues and operating results for any interim quarter are generally not indicative of the revenues and operating results for the year and may not be comparable with results for the corresponding period of the previous year. The Company conducts the majority of its live racing during the second, third and fourth quarters, including the running of the Kentucky Derby and the Kentucky Oaks during the second quarter, the quarter during which the Company typically generates the majority of its annual operating income. The Company conducted 111 live racing days during the third quarter of 2010, which compares to 118 live racing days conducted during the third quarter of 2009. For the nine months ended September 30, 2010, the Company conducted 278 live racing days, which compares to 297 live racing days conducted during the nine months ended September 30, 2009.

**Comprehensive Earnings**

The Company had no other components of comprehensive earnings and, as such, comprehensive earnings is the same as net earnings as presented in the accompanying Condensed Consolidated Statements of Net Earnings.

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**NOTE 2 — DISCONTINUED OPERATIONS**

During September 2010, the Company committed to a plan to dissolve Churchill Downs Entertainment Group, (“CDE”), an entity created to conceive and produce large-scale entertainment events. The decision was made to dissolve the group because of our belief that achieving financial success conducting large-scale entertainment events is very difficult in the current economy.

Financial Information

CDE, Ellis Park and Hollywood Park have been accounted for as discontinued operations. Accordingly, the results of operations of the dissolved and sold businesses for all periods presented have been classified as discontinued operations, net of income taxes, in the Condensed Consolidated Statements of Net (Loss) Earnings. Set forth below is a summary of the results of operations of the dissolved and sold businesses for the three and nine months ended September 30, 2010 and 2009 (in thousands):

|  | Three Months Ended<br>September 30, |                  | Nine Months Ended<br>September 30, |                 |
|--|-------------------------------------|------------------|------------------------------------|-----------------|
|  | 2010                                | 2009             | 2010                               | 2009            |
| Net revenues   | \$ 6,303                            | \$ —             | \$ 6,303                           | \$ —            |
| Operating expenses   | 11,921                              | —                | 12,793                             | —               |
| Selling, general and administrative expenses                                     | 1,389                               | —                | 2,060                              | —               |
| Operating loss   | (7,007)                             | —                | (8,550)                            | —               |
| Other income (expense):  |                                     |                  |                                    |                 |
| Miscellaneous, net   | —                                   | (46)             | 69                                 | 362             |
|  | —                                   | (46)             | 69                                 | 362             |
| (Loss) earnings from continuing operations before income tax benefit (provision) | (7,007)                             | (46)             | (8,481)                            | 362             |
| Income tax benefit (provision)   | 2,618                               | (1,063)          | 2,904                              | (1,225)         |
| Net loss   | <u>\$ (4,389)</u>                   | <u>\$(1,109)</u> | <u>\$ (5,577)</u>                  | <u>\$ (863)</u> |

Set forth below is a summary of the net assets held for dissolution, which relate to CDE, as of September 30, 2010 (in thousands):

|   | September 30,<br>2010 |
|---|-----------------------|
| Assets held for dissolution                             | \$ —                  |
| Current liabilities:                                    |                       |
| Accrued severance expense                               | 760                   |
| Other accrued expenses                                  | 329                   |
| Liabilities associated with assets held for dissolution | <u>\$ 1,089</u>       |

**NOTE 3 — HOOSIER PARK CONSIDERATION**

In accordance with the sale of the Company’s 62% ownership interest in Hoosier Park, L.P. (“Hoosier Park”) to Centaur Racing, LLC (“Centaur”), on March 30, 2007, the Company received a promissory note issued, jointly and severally, by three individual investors in Centaur (the “Note”) in the amount of \$4.0 million, which accrued interest at a rate of 8.25% per year. According to the terms of the Note, interest was due and payable in one lump sum upon maturity of the note on March 30, 2010. As of September 30, 2010, approximately \$5.1 million of principal and interest is outstanding in accordance with the Note terms. The Company has determined that the amount outstanding is collectible and that no allowance is deemed necessary as of September 30, 2010.

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

The Partnership Interest Purchase Agreement with Centaur includes a contingent consideration provision whereby the Company is entitled to payments of up to \$15 million on the date which is eighteen months after the date that slot machines are operational at Hoosier Park. During June 2008, Hoosier Park commenced its slot operations, fulfilling the terms of the contingency provision. As of September 30, 2010, the Company has determined that collectability of amounts due under the contingent consideration provision is not reasonably assured and, therefore, has not recognized the amounts due under the Partnership Interest Purchase Agreement. Amounts due will be recorded as a gain on the sale of Hoosier Park once collectability is reasonably assured.

**NOTE 4 — ACQUISITIONS**

Harlow’s Casino Resort & Hotel Acquisition

During September 2010, the Company announced that it had entered into a definitive purchase agreement to acquire Harlow’s Casino Resort & Hotel in Greenville, Mississippi in a transaction valued at approximately \$138.0 million. The Company expects to finance the purchase price with borrowings under its revolving credit facility. The transaction is subject to receipt of all required regulatory approvals, including securing a gaming license in Mississippi, obtaining approval from its lenders under the revolving credit facility and other customary closing conditions. Closing is expected to occur during the fourth quarter of 2010 or the first quarter of 2011.

Youbet Acquisition

On June 2, 2010, the Company completed its acquisition of Youbet.com, Inc. (“Youbet”) pursuant to an Agreement and Plan of Merger dated as of November 11, 2009 for an aggregate purchase price of \$131.8 million, which consisted of \$45.3 million of cash and approximately 2.7 million shares of the Company’s common stock valued at \$86.5 million based on the closing price of the Company’s common stock on June 1, 2010 of \$32.04. The transaction included the acquisition of the account wagering platform of Youbet and the operations of United Tote Company and United Tote Canada (collectively “United Tote”), which manufactures and operates pari-mutuel wagering systems for approximately 100 racetracks, off-track betting facilities (“OTBs”) and other pari-mutuel wagering businesses. The primary reason for the acquisition was to invest in assets with an expected yield on investment and continue the Company’s growth in one of the fastest growing segments of the pari-mutuel industry.

The acquisition of Youbet was accounted for under the purchase method. The following table summarizes the preliminary estimated fair values of the assets acquired and liabilities assumed at the date of the acquisition. Such estimates are subject to refinement as additional valuation information is received.

|                                      | <u>Total</u>     |
|--------------------------------------|------------------|
| Restricted cash                      | \$ 5,544         |
| Accounts receivable, net             | 2,761            |
| Prepaid expenses                     | 984              |
| Inventory                            | 1,020            |
| Other assets                         | 103              |
| Property and equipment               | 9,063            |
| Deferred income taxes                | 30,663           |
| Goodwill                             | 68,045           |
| Other intangible assets              | <u>27,300</u>    |
| Total assets acquired                | 145,483          |
| Accounts payable                     | 11,140           |
| Accrued expenses                     | 4,609            |
| Deferred revenue                     | 299              |
| Income taxes payable                 | (941)            |
| Deferred income taxes                | <u>11,471</u>    |
| Total liabilities acquired           | 26,578           |
| Purchase price, net of cash acquired | <u>\$118,905</u> |

Depreciation of property and equipment acquired is calculated using the straight-line method over the estimated useful lives of the related assets as follows: 3 to 5 years for computer hardware and software, 5 to 10 years for equipment, 7 years for

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

furniture and fixtures and 1 to 7 years for leasehold improvements. Amortization of other intangible assets acquired is calculated using the straight-line method over the estimated useful life of the related intangible asset. Other intangible assets primarily consist of three segments of customer relationships valued at \$15.1 million, \$4.6 million and \$7.0 million with lives of 7 years, 6 years and 5 years, respectively. The entire balance of goodwill, which includes expected synergies from combining the operations of Youbet and the Company, has been allocated to the Online Business segment. The Company does not expect to deduct any portion of goodwill for income tax purposes.

During the nine months ended September 30, 2010, the Company recognized an impairment loss of \$1.3 million associated with software owned by TwinSpires. The Company determined such software would not be utilized as a result of a reassessment of the use of certain technology in connection with its acquisition of Youbet.

On September 28 and 29, 2010, the Company provided notices to 36 employees that their employment will likely be terminated effective on or around December 3, 2010. The Company also informed 23 other employees that their employment will likely be terminated between December 31, 2010 and January 31, 2011, and informed 5 employees that their employment will likely be terminated during the period of 3 to 12 months after December 31, 2010. Certain of these employees have already received or may receive offers to relocate to another division of the Company at one of the Company's other facilities.

These employee separations were prompted by the identification of redundancies in the Company's Online Business as a result of the Company's merger with Youbet, which was completed on June 2, 2010, and this action is one of the Company's undertakings to achieve the \$12 million in anticipated annualized cost synergies in connection with the Company's acquisition and integration of Youbet, as previously disclosed. During the three months ended September 30, 2010, in accordance with the terms of a historic, ongoing benefit arrangement, the Company recognized \$1.2 million of severance and other benefits costs, which are included within selling, general and administrative expenses in the Condensed Consolidated Statement of Net (Loss) Earnings.

Pro Forma

The following table illustrates the effect on net revenues, earnings from continuing operations and earnings from continuing operations per common share as if the Company had consummated the merger with Youbet as of the beginning of each period presented. The pro forma results have been prepared for comparative purposes only and do not purport to be indicative of the results of operations that would have occurred had the merger with Youbet been consummated at the beginning of the respective periods.

|  | Three Months Ended    | Nine Months Ended     |           |
|--|-----------------------|-----------------------|-----------|
|  | September 30,<br>2009 | September 30,<br>2010 | 2009      |
| Net revenues   | \$ 128,772            | \$457,724             | \$440,777 |
| Earnings from continuing operations  | (627)                 | 22,362                | 27,787    |
| Earnings from continuing operations per common share                           |                       |                       |           |
| Basic:   |                       |                       |           |
| Earnings from continuing operations  | \$ (0.04)             | \$ 1.33               | \$ 1.66   |
| Diluted:   |                       |                       |           |
| Earnings from continuing operations  | \$ (0.04)             | \$ 1.33               | \$ 1.66   |
| Shares used in computing earnings from continuing operations per common share: |                       |                       |           |
| Basic  | 16,287                | 16,309                | 16,278    |
| Diluted  | 16,287                | 16,770                | 16,740    |

During the three months ended September 30, 2010, Youbet and United Tote contributed total revenues of \$25.3 million and earnings before income tax provision of \$0.4 million, to the Company's reported results included in the Condensed Consolidated Statement of Net Earnings. During the nine months ended September 30, 2010, Youbet and United Tote contributed total revenues of \$34.0 million and earnings before income tax provision of \$0.4 million, to the Company's reported results included in the Condensed Consolidated Statement of Net Earnings.

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)**

**NOTE 5 — SETTLEMENT WITH ODS**

On July 2, 2010, the Company entered into an agreement with ODS Technologies, LP (d/b/a TVG) (“ODS”), settling a dispute arising under the License and Content Agreement dated as of May 18, 2001, as subsequently amended and modified, between TVG and ODS (the “Agreement”). As part of the settlement, the Agreement was terminated and the Company received a one-time, payment of \$1.3 million, which was recognized as miscellaneous income during the third quarter of 2010.

**NOTE 6 — INCOME TAXES**

The Company recently underwent a federal income tax audit for calendar years 2004 through 2008.

During 2005 and 2006, the Company received approximately \$23.5 million of proceeds related to the sale of Personal Seat Licenses (“PSLs”) sold in connection with the renovation of Churchill Downs Racetrack (“Churchill Downs”). The PSLs that were sold included those with terms of 30 years and 5 years and provided the purchaser the right to purchase tickets to the Kentucky Derby, Kentucky Oaks and Breeders’ Cup races each year during the term of the license. Accordingly, for tax purposes, the Company deferred the income for the PSLs over the respective terms of the licenses.

During 2009, the Internal Revenue Service (the “IRS”) proposed that the income related to the sale of the PSLs is taxable during the period the proceeds were received by the Company (the “Proposed Audit Adjustment”). As a result, the Proposed Audit Adjustment served to increase the amount of income taxes due for each of the tax years 2005 and 2006.

On April 14, 2010, the Company defended its position of deferring income related to the sale of PSLs using a fast track mediation process offered by the IRS. During the fast track mediation process, the Company agreed to change its method of accounting for proceeds related to the sale of PSLs to the deferral method provided for in Revenue Procedure 2004-34, effective for the taxable year ended December 31, 2007. As a result, the Company’s taxable income for each of the years ended December 31, 2007 and 2008 will increase by \$19.1 million and \$0.4 million, respectively. In accordance with the settlement entered into during the fast track mediation process, the Company recognized an income tax benefit from continuing operations of \$1.6 million during the nine months ended September 30, 2010 reflecting a reduction of interest expense previously estimated and recognized during 2009 as a result of the Proposed Audit Adjustment.

As of September 30, 2010, the Company had gross unrecognized income tax benefits of \$2.3 million. Additionally, the Company recognized income tax benefits related to uncertain tax positions of \$0.2 million for each of the three and nine months ended September 30, 2010. The Company anticipates a decrease in its unrecognized income tax benefits of approximately \$0.5 million over the next twelve months. The anticipated decrease is primarily due to the expiration of statutes in various jurisdictions.

The Company recognizes accrued interest related to unrecognized income tax benefits in income tax expense and penalties in selling, general and administrative expenses in the Condensed Consolidated Statements of Net (Loss) Earnings. As of September 30, 2010, the Company had accrued \$0.2 million of interest related to unrecognized income tax benefits.

The timing of any payments for any related state tax deficiencies will generally follow closely after the timing of any federal payments.

**NOTE 7 — GOODWILL AND INDEFINITE-LIVED INTANGIBLE ASSETS IMPAIRMENT TEST**

Goodwill and indefinite-lived intangible assets are tested for impairment on an annual basis. In assessing whether goodwill is impaired, the fair value of the related reporting unit is compared to its carrying amount, including goodwill. If the carrying amount of the reporting unit exceeds its fair value, the second step of the goodwill impairment test is performed to measure the amount of impairment loss, if any. The second step of the goodwill impairment test consists of comparing the implied fair value of reporting unit goodwill with the carrying amount of that goodwill. If the carrying amount of reporting unit goodwill exceeds the implied fair value of that goodwill, an impairment loss is recognized equal to such excess. The implied fair value of goodwill is determined in the same manner as when determining the amount of goodwill recognized in a business combination. The Company completed the required annual impairment tests of goodwill and indefinite-lived intangible assets during the three months ended March 31, 2010, and no adjustment to the carrying value of goodwill or indefinite-lived intangible assets was required.

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)**

**NOTE 8 — FAIR VALUE OF FINANCIAL INSTRUMENTS**

The Company adheres to a hierarchy for ranking the quality and reliability of the information used to determine fair values. Assets and liabilities that are carried at fair value are classified and disclosed in one of the following three categories:

Level 1: Unadjusted quoted market prices in active markets for identical assets or liabilities.

Level 2: Unadjusted quoted prices in active markets for similar assets or liabilities, unadjusted quoted prices for identical or similar assets or liabilities in markets that are not active, or inputs other than quoted prices that are observable for the asset or liability.

Level 3: Unobservable inputs for the asset or liability.

In January 2010, the Financial Accounting Standards Board (“FASB”) issued authoritative guidance on improving disclosures about fair value measurements. This guidance requires new disclosures about transfers in and out of Level 1 and 2 measurements and separate disclosures about activity relating to Level 3 measurements. In addition, this guidance clarifies existing fair value disclosures about the level of disaggregation and the input and valuation techniques used to measure fair value. The guidance only relates to disclosure and does not impact the Company’s condensed consolidated financial statements. The Company adopted this guidance during the first quarter of 2010. There was no significant impact to the Company’s disclosures upon adoption.

The Company endeavors to utilize the best available information in measuring fair value. Financial assets and liabilities are classified based on the lowest level of input that is significant to the fair value measurement. Approximately \$2.5 million of the Company’s cash equivalents and restricted cash as of September 30, 2010, which are held in interest bearing accounts, are recorded based on Level 1 inputs. The Company currently has no other assets or liabilities subject to fair value measurement on a recurring basis.

The following methods and assumptions were used by the Company in estimating its fair value disclosures for financial instruments:

**Cash Equivalents**—The carrying amount reported in the balance sheet for cash equivalents approximates its fair value due to the short-term maturity of these instruments.

**Long-term Debt**—The carrying amounts of the Company’s borrowings under its line of credit agreements and other long-term debt approximates fair value, based upon current interest rates.

**Convertible Note Payable, Related Party**—The fair value of the convertible note payable, related party and the related embedded derivative instruments are estimated using pricing models similar to those used to value stock options. The Company determined it was not practicable to estimate the fair value of the Convertible Note Payable, related party, as a quoted market price is not available and the cost of obtaining an independent valuation is excessive. The principal amount of the Convertible Note Payable, related party, is \$16.7 million, and it matures on October 18, 2014.

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

**NOTE 9 — EARNINGS PER COMMON SHARE COMPUTATIONS**

The following is a reconciliation of the numerator and denominator of the earnings per common share computations (in thousands, except per share data):

|   | <u>Three Months Ended</u><br><u>September 30,</u> |                   | <u>Nine Months Ended</u><br><u>September 30,</u> |                 |
|---|---|-------------------|--|-----------------|
|   | <u>2010</u>                                       | <u>2009</u>       | <u>2010</u>                                      | <u>2009</u>     |
| <b>Numerator for basic earnings (loss) from continuing operations per common share:</b> |   |                   |  |                 |
| Earnings (loss) from continuing operations  | \$ 3,700  | \$ (1,216)        | \$23,825   | \$24,573        |
| Earnings (loss) from continuing operations allocated to participating securities        | (100)   | —                 | (707)  | (793)           |
| Numerator for basic earnings (loss) from continuing operations per common share         | <u>\$ 3,600</u>                                   | <u>\$ (1,216)</u> | <u>\$23,118</u>                                  | <u>\$23,780</u> |
| <b>Numerator for basic net (loss) earnings per common share:</b>                        |   |                   |  |                 |
| Net (loss) earnings   | \$ (689)  | \$ (2,325)        | \$18,248   | \$23,710        |
| Net loss allocated to participating securities  | —   | —                 | (542)  | (765)           |
| Numerator for basic net (loss) earnings per common share                                | <u>\$ (689)</u>                                   | <u>\$ (2,325)</u> | <u>\$17,706</u>                                  | <u>\$22,945</u> |
| <b>Numerator for diluted net (loss) earnings per common share:</b>                      |   |                   |  |                 |
| Earnings (loss) from continuing operations  | \$ 3,700  | \$ (1,216)        | \$23,825   | \$24,573        |
| Discontinued operations, net of income taxes  | (4,389)   | (1,109)           | (5,577)  | (863)           |
| Net (loss) earnings   | <u>\$ (689)</u>                                   | <u>\$ (2,325)</u> | <u>\$18,248</u>                                  | <u>\$23,710</u> |
| <b>Denominator for net (loss) earnings per common share:</b>                            |   |                   |  |                 |
| Basic   | 16,311  | 13,587            | 14,796   | 13,578          |
| Plus dilutive effect of stock options   | 4   | —                 | 8  | 9               |
| Plus dilutive effect of convertible note  | 453   | —                 | 453  | 453             |
| Diluted   | <u>16,768</u>                                     | <u>13,587</u>     | <u>15,257</u>                                    | <u>14,040</u>   |
| <b>(Loss) earnings per common share:</b>  |   |                   |  |                 |
| <b>Basic</b>  |   |                   |  |                 |
| Earnings (loss) from continuing operations  | \$ 0.22   | \$ (0.09)         | \$ 1.56  | \$ 1.75         |
| Discontinued operations   | (0.26)  | (0.08)            | (0.36)   | (0.06)          |
| Net (loss) earnings   | <u>\$ (0.04)</u>                                  | <u>\$ (0.17)</u>  | <u>\$ 1.20</u>                                   | <u>\$ 1.69</u>  |
| <b>Diluted</b>  |   |                   |  |                 |
| Earnings (loss) from continuing operations  | \$ 0.22   | \$ (0.09)         | \$ 1.56  | \$ 1.75         |
| Discontinued operations   | (0.26)  | (0.08)            | (0.36)   | (0.06)          |
| Net (loss) earnings   | <u>\$ (0.04)</u>                                  | <u>\$ (0.17)</u>  | <u>\$ 1.20</u>                                   | <u>\$ 1.69</u>  |

Options to purchase approximately 191 thousand shares and 137 thousand shares for the three and nine months ended September 30, 2010 are excluded from the computation of earnings from continuing operations per common share assuming dilution because the options' exercise prices were greater than the average market price of the common shares.

Options to purchase approximately 112 thousand shares for the nine months ended September 30, 2009 are excluded from the computation of earnings from continuing operations per common share assuming dilution because the options' exercise prices were greater than the average market price of the common shares. Options to purchase approximately eight thousand shares for the three months ended September 30, 2009 are excluded from the computation of diluted net loss from continuing operations per common share since their effect is antidilutive because of the net loss from continuing operations for the period. Also, 453 thousand shares issuable upon conversion of notes payable for the three months ended September 30, 2009 are excluded from the computation of diluted net loss from continuing operations per common share since their effect is antidilutive because of the net loss for the period.

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)**

**NOTE 10 — SEGMENT INFORMATION**

The Company operates in the following four segments: (1) Racing Operations, which includes Churchill Downs, Calder Race Course, Arlington Park Race Course and its ten OTBs and Fair Grounds Race Course and the pari-mutuel activity generated at its eleven OTBs; (2) Online Business, which includes TwinSpires, our Advance Deposit Wagering (“ADW”) business, Youbet.com, LLC, an ADW business acquired on June 2, 2010, and Bloodstock Research Information Services, as well as the Company’s equity investment in HRTV, LLC; (3) Gaming, which includes video poker and gaming operations at Fair Grounds Slots and Calder Casino and Video Services, Inc., an owner and operator of more than 800 video poker machines in Louisiana; and (4) Other Investments, which includes United Tote, a manufacturer and operator of pari-mutuel wagering systems acquired by the Company on June 2, 2010, Churchill Downs Simulcast Productions and the Company’s other minor investments. Eliminations include the elimination of intersegment transactions.

The accounting policies of the segments are the same as those described in the “Summary of Significant Accounting Policies” in Note 1 to the consolidated financial statements included in the Company’s Annual Report on Form 10-K for the year ended December 31, 2009. The Company uses revenues and EBITDA (defined as earnings before interest, taxes, depreciation and amortization) as key performance measures of the results of operations for purposes of evaluating performance internally. Furthermore, management believes that the use of these measures enables management and investors to evaluate and compare from period to period the Company’s operating performance in a meaningful and consistent manner. Because the Company uses EBITDA as a key performance measure of financial performance, the Company provides a reconciliation of its calculation of EBITDA to net earnings. However, these measures should not be considered as an alternative to, or more meaningful than, net earnings (as determined in accordance with accounting principles generally accepted in the United States of America) as a measure of the Company’s operating results or cash flows (as determined in accordance with accounting principles generally accepted in the United States of America) as a measure of the Company’s liquidity.

EBITDA of the corporate segment includes approximately \$0.5 million of management fees for the three and nine months ended September 30, 2010 related to the dissolution of CDE which is included in discontinued operations.

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

The table below presents information about reported segments for the three and nine months ended September 30, 2010 and 2009 (in thousands):

|   | Three Months Ended<br>September 30, |                   | Nine Months Ended<br>September 30, |                  |
|---|-------------------------------------|-------------------|------------------------------------|------------------|
|   | 2010                                | 2009              | 2010                               | 2009             |
| <b>Net revenues from external customers:</b>                    |                                     |                   |                                    |                  |
| Churchill Downs   | \$ 5,449                            | \$ 5,226          | \$ 96,979                          | \$ 95,718        |
| Arlington Park  | 29,445                              | 33,935            | 61,533                             | 75,337           |
| Calder  | 21,604                              | 22,663            | 42,848                             | 44,295           |
| Fair Grounds  | 5,942                               | 6,534             | 32,367                             | 35,262           |
| Total Racing Operations   | 62,440                              | 68,358            | 233,727                            | 250,612          |
| Online Business   | 38,739                              | 17,386            | 86,089                             | 54,830           |
| Gaming  | 28,306                              | 14,104            | 82,824                             | 47,368           |
| Other Investments   | 6,195                               | 963               | 8,599                              | 1,320            |
| Corporate   | 64                                  | 85                | 67                                 | 540              |
| Net revenues from external customers                            | <u>\$135,744</u>                    | <u>\$100,896</u>  | <u>\$411,306</u>                   | <u>\$354,670</u> |
| <b>Intercompany net revenues:</b>                               |                                     |                   |                                    |                  |
| Churchill Downs   | \$ 336                              | \$ 233            | \$ 2,872                           | \$ 2,438         |
| Arlington Park  | 1,199                               | 800               | 2,542                              | 1,637            |
| Calder  | 557                                 | 381               | 932                                | 743              |
| Fair Grounds  | 39                                  | 11                | 586                                | 591              |
| Total Racing Operations   | 2,131                               | 1,425             | 6,932                              | 5,409            |
| Online Business   | 112                                 | 150               | 533                                | 448              |
| Other Investments   | 629                                 | 386               | 1,604                              | 1,286            |
| Eliminations  | (2,872)                             | (1,961)           | (9,069)                            | (7,143)          |
| Net revenues  | <u>\$ —</u>                         | <u>\$ —</u>       | <u>\$ —</u>                        | <u>\$ —</u>      |
| <b>Reconciliation of Segment EBITDA to net (loss) earnings:</b> |                                     |                   |                                    |                  |
| Racing Operations   | \$ 1,254                            | \$ 3,428          | \$ 37,819                          | \$ 41,174        |
| Online Business   | 5,818                               | 2,802             | 14,467                             | 11,767           |
| Gaming  | 7,892                               | 3,884             | 19,537                             | 15,401           |
| Other Investments   | 1,792                               | 831               | 2,918                              | 1,651            |
| Corporate   | 296                                 | (1,208)           | (2,327)                            | (2,606)          |
| Total EBITDA  | 17,052                              | 9,737             | 72,414                             | 67,387           |
| Depreciation and amortization                                   | (12,395)                            | (7,523)           | (34,410)                           | (22,399)         |
| Interest (expense) income, net                                  | (1,595)                             | 148               | (4,145)                            | 8                |
| Income tax benefit (provision)                                  | 638                                 | (3,578)           | (10,034)                           | (20,423)         |
| Earnings (loss) from continuing operations                      | 3,700                               | (1,216)           | 23,825                             | 24,573           |
| Discontinued operations, net of income taxes                    | (4,389)                             | (1,109)           | (5,577)                            | (863)            |
| Net (loss) earnings   | <u>\$ (689)</u>                     | <u>\$ (2,325)</u> | <u>\$ 18,248</u>                   | <u>\$ 23,710</u> |

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
(Unaudited)

The table below presents information about equity in earnings and losses of unconsolidated investments included in the Company's reported segments for the three and nine months ended September 30, 2010 and 2009 (in thousands):

|                   | Three Months Ended<br>September 30, |                 | Nine Months Ended<br>September 30, |                 |
|-------------------|-------------------------------------|-----------------|------------------------------------|-----------------|
|                   | 2010                                | 2009            | 2010                               | 2009            |
| Online Business   | \$ (543)                            | \$ (490)        | \$ (345)                           | \$ (536)        |
| Other Investments | 73                                  | (78)            | 28                                 | (105)           |
|                   | <u>\$ (470)</u>                     | <u>\$ (568)</u> | <u>\$ (317)</u>                    | <u>\$ (641)</u> |

The table below presents total asset information for reported segments (in thousands):

|                      | September 30,     | December 31,      |
|----------------------|-------------------|-------------------|
|                      | 2010              | 2009              |
| <b>Total assets:</b> |                   |                   |
| Racing Operations    | \$ 779,390        | \$ 645,933        |
| Online Business      | 197,291           | 88,664            |
| Gaming               | 110,316           | 107,128           |
| Other Investments    | 190,124           | 178,707           |
|                      | 1,277,121         | 1,020,432         |
| Eliminations         | (427,190)         | (295,030)         |
|                      | <u>\$ 849,931</u> | <u>\$ 725,402</u> |

The table below presents total goodwill information for reported segments (in thousands):

|                   | September 30,     | December 31,      |
|-------------------|-------------------|-------------------|
|                   | 2010              | 2009              |
| <b>Goodwill:</b>  |                   |                   |
| Racing Operations | \$ 50,401         | \$ 50,401         |
| Online Business   | 128,608           | 60,563            |
| Gaming            | 3,127             | 3,127             |
| Other Investments | 1,258             | 1,258             |
|                   | <u>\$ 183,394</u> | <u>\$ 115,349</u> |

The table below presents total capital expenditure information for reported segments (in thousands):

|                                   | Nine Months Ended<br>September 30, |                 |
|-----------------------------------|------------------------------------|-----------------|
|                                   | 2010                               | 2009            |
| <b>Capital expenditures, net:</b> |                                    |                 |
| Racing Operations                 | \$33,825                           | \$ 6,497        |
| Online Business                   | 3,842                              | 1,578           |
| Gaming                            | 16,667                             | 23,102          |
| Other Investments                 | 2,159                              | 1,128           |
|                                   | <u>\$56,493</u>                    | <u>\$32,305</u> |

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)**

**NOTE 11 — RELATED PARTY TRANSACTIONS**

During 2009, the Company entered into an agreement with The Duchossois Group (“TDG”), a related party, for the purchase of real estate adjacent to Arlington Park. TDG beneficially owns more than 5% of the Company’s common stock. The total purchase price of \$27.5 million was financed by a cash payment of \$3.5 million and a non-interest bearing promissory note of \$24.0 million. During the nine months ended September 30, 2010, the Company fully repaid the promissory note balance of \$24.0 million in accordance with the original terms of the promissory note.

**NOTE 12 – DISSOLUTION OF TRACKNET MEDIA GROUP LLC**

During 2007, together with Magna Entertainment Corporation (“MEC”), the Company formed a venture, TrackNet Media Group LLC (“TrackNet”) through which horseracing content was made readily available through a variety of distribution points and wagering platforms in order to enhance growth within the industry. TrackNet ceased operations during the nine months ended September 30, 2010, and each party will now be responsible for buying and selling its own horseracing content. All existing third-party content agreements involving TrackNet were entered into by TrackNet as an agent for each Company-owned and MEC-owned racetrack. Accordingly, those contracts, and their underlying rights and obligations, will continue to be valid for the remainder of the contracts’ respective terms. There was no significant impact on the Company’s consolidated financial position or results of operations for the three and nine months ended September 30, 2010 as a result of ceasing operations.

**NOTE 13 — COMMITMENTS AND CONTINGENCIES**

**Acquisition of Youbet**

On November 17, 2009, a putative class action lawsuit, *Wayne Witkowski v. Youbet.com, Inc., et al.*, was filed in the Superior Court of Los Angeles, California against Youbet, various of its directors, the Company and the Company’s wholly-owned subsidiaries, Tomahawk Merger Corp. (“Merger Sub”) and Tomahawk Merger LLC (“Merger LLC”). Subsequently, five additional lawsuits were also filed in the Los Angeles Superior Court, two of which name Youbet and its directors as defendants and three of which also name the Company as a defendant. All six lawsuits (collectively, the “Los Angeles Litigation”), are putative class actions brought on behalf of Youbet’s stockholders. Plaintiffs in the Los Angeles Litigation moved to consolidate the Los Angeles Litigation, to file a single consolidated complaint and to appoint lead counsel. That motion was granted on January 22, 2010.

The complaints in the Los Angeles Litigation all allege that Youbet’s directors breached their fiduciary duties, including alleged duties of loyalty, due care and candor, in connection with the sale of Youbet. In that regard, the various complaints include, among other things, allegations that the sale of Youbet is the result of an inadequate sales process which has not been designed to maximize stockholder value; that the consideration to be received by Youbet stockholders is unfair and inadequate; that the merger agreement includes inappropriate “no solicitation,” “matching rights,” no standstill waiver, and termination fee provisions; that the combined effect of these provisions, together with Youbet’s waiver of the Youbet stockholder rights agreement with respect to the Company and the entry of voting agreements by defendants and certain others pursuant to which they have agreed to vote in favor of the sale of Youbet, was to “lock up” the sale of Youbet, foreclose potential alternative bidders and illegally restrain Youbet’s ability to solicit or engage in negotiations with a third party; that various defendants acted for their own benefit in approving the sale of Youbet, including for the purpose of obtaining positions or pursuing opportunities at the Company; and that material information was not provided in connection with the sale of Youbet and was not provided at the time that Youbet submitted the Youbet stockholder rights agreement to a stockholder vote. Those lawsuits which name the Company or its affiliates as defendants also allege that the Company has aided and abetted the alleged breaches of fiduciary duty by Youbet’s directors. Youbet is also alleged to have aided and abetted the alleged breaches of fiduciary duty by its directors. Among the relief sought by the complaints is an enjoining of the sale of Youbet, or unspecified damages, together with payment of attorneys’ fees and costs.

On December 23, 2009, a putative class action lawsuit, *Raymond Balch v. Youbet.com, Inc., et al.*, was filed in the Delaware Court of Chancery against Youbet, various of its directors, the Company, Merger Sub and Merger LLC alleging claims similar to the Los Angeles Litigation. On January 8, 2010, Mr. Balch amended his complaint to add counts asserting that Youbet’s directors breached their fiduciary duties to Youbet stockholders by allegedly failing to disclose material information regarding the sale of Youbet in a preliminary registration statement filed with the Securities and Exchange Commission on December 24, 2009 and that Youbet and the Company aided and abetted such alleged breaches.

NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)

On March 2, 2010, Youbet, Youbet's directors, the Company, Merger Sub, and Merger LLC entered into a memorandum of understanding with the plaintiffs in the Los Angeles Litigation and the plaintiffs in the *Balch* litigation reflecting an agreement in principle to settle the cases based on, among other things, defendants' agreement to include in an amended registration statement certain additional disclosures relating to the sale of Youbet. The memorandum of understanding provides that the settlement is subject to customary conditions including the completion of appropriate settlement documentation and completion of confirmatory discovery. Pursuant to the memorandum of understanding, an amended registration statement was filed containing the additional agreed disclosures.

On or about July 14, 2010, the parties to the Los Angeles Litigation and the *Balch* litigation entered into a settlement agreement consistent with the terms of the memorandum of understanding. The settlement agreement provides, among other things, for a certification of a class for settlement purposes, dismissal with prejudice of the Los Angeles Litigation and the *Balch* litigation, releases by class members and payment of attorneys' fees and expenses approved by the court. The settlement agreement is subject to court approval. In both the memorandum of understanding and the settlement agreement, Youbet, Youbet's directors, the Company, Merger Sub, and Merger LLC each deny that they have committed or aided and abetted in the commission of any violation of law or engaged in any of the wrongful acts alleged in the complaints, and expressly maintain that they diligently and scrupulously complied with any and all of their legal duties. Although Youbet, Youbet's directors, the Company, Merger Sub, and Merger LLC believe the lawsuits are without merit, they entered into the memorandum of understanding and settlement to eliminate the burden and expense of further litigation. On July 14, 2010, plaintiffs in the Los Angeles Litigation filed the settlement agreement with the Superior Court of California, County of Los Angeles, together with a request for preliminary approval of the settlement and of a proposed class notice and for the scheduling of a hearing date for final approval of the settlement. On August 19, 2010, the court presiding over the Los Angeles litigation granted preliminary approval to the proposed settlement and scheduled a final approval hearing dated December 20, 2010.

If the settlement is consummated, the Los Angeles Litigation and the *Balch* litigation will each be dismissed with prejudice and the defendants and other released persons will receive from or on behalf of all of Youbet's non-affiliated public stockholders who held Youbet common stock at any time from November 10, 2009 through the date of the consummation of the merger a release of, among other things, all claims relating to the sale of Youbet, the merger agreement and the transactions contemplated therein, disclosures made relating to the sale of Youbet, and any compensation or other payments made to the defendants in connection with the sale of Youbet. The release does not apply to the right of any Youbet stockholder or former Youbet stockholder who has taken the steps required by Delaware law to seek appraisal of his or her Youbet shares from pursuing an appraisal in accordance with Delaware law. Plaintiffs will also receive a release from the defendants with respect to all claims arising out of, relating to, or in connection with the institution, prosecution, assertion or resolution of the lawsuits. The Company will not incur any significant loss or expense as a result of this settlement.

Receipt of Illinois Riverboat Subsidy

During 2009, the Company received a payment of \$24.0 million from the Horse Racing Equity Trust Fund ("HRTE Trust Fund") related to subsidies paid by Illinois riverboat casinos in accordance with Public Act 94-804. During the nine months ended September 30, 2010, the Company received an additional \$14.6 million from the HRTE Trust Fund. The monies have been placed into an escrow account of Arlington Park and are recognized as restricted cash. Revenues from these subsidies continue to be deferred as of September 30, 2010, as challenges regarding the constitutionality of Public Act 94-804 are still being made by the Illinois riverboat casinos.

**NOTE 14 — AMENDMENT OF REVOLVING CREDIT FACILITY**

On November 1, 2010, the Company entered into Amendment No. 1 to the Second Amended and Restated Credit Agreement (the "Amendment"), which amends certain provisions of the credit agreement and provides for the exercise of the accordion feature whereby the maximum aggregate commitment will be increased from \$275 million to \$375 million. Additionally, the Amendment reduces the pricing schedule for outstanding borrowings by 37.5 basis points and commitment fees by 5 basis points across all leverage pricing levels. The guarantors under the credit agreement continue to be a majority of the Company's wholly-owned subsidiaries. The Company incurred loan origination costs of approximately \$0.4 million in connection with the Amendment, which will be capitalized and will be amortized as interest expense over the remaining term of the credit agreement. The facility terminates on December 22, 2013.

**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS  
(Unaudited)**

Generally, borrowings made pursuant to the Amendment will bear interest at a LIBOR-based rate per annum plus an applicable percentage ranging from 1.625% to 3.125% depending on certain of the Company's financial ratios. In addition, under the Amendment, the Company agreed to pay a commitment fee at rates that range from 0.25% to 0.45% of the available aggregate commitment, depending on the Company's leverage ratio.

**ITEM 2. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

Information set forth in this discussion and analysis contains various “forward-looking statements” within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934. The Private Securities Litigation Reform Act of 1995 (the “Act”) provides certain “safe harbor” provisions for forward-looking statements. All forward-looking statements made in this Quarterly Report on Form 10-Q are made pursuant to the Act. The reader is cautioned that such forward-looking statements are based on information available at the time and/or management’s good faith belief with respect to future events, and are subject to risks and uncertainties that could cause actual performance or results to differ materially from those expressed in the statements. Forward-looking statements speak only as of the date the statement was made. We assume no obligation to update forward-looking information to reflect actual results, changes in assumptions or changes in other factors affecting forward-looking information. Forward-looking statements are typically identified by the use of terms such as “anticipate,” “believe,” “could,” “estimate,” “expect,” “intend,” “may,” “might,” “plan,” “predict,” “project,” “should,” “will,” and similar words, although some forward-looking statements are expressed differently. Although we believe that the expectations reflected in such forward-looking statements are reasonable, we can give no assurance that such expectations will prove to be correct. Important factors that could cause actual results to differ materially from expectations include: the effect of global economic conditions, including any disruptions in the credit markets; the effect (including possible increases in the cost of doing business) resulting from future war and terrorist activities or political uncertainties; the overall economic environment; the impact of increasing insurance costs; the impact of interest rate fluctuations; the effect of any change in our accounting policies or practices; the financial performance of our racing operations; the impact of gaming competition (including lotteries, on-line gaming and riverboat, cruise ship and land-based casinos) and other sports and entertainment options in those markets in which we operate; the impact of live racing day competition with other Florida, Illinois and Louisiana racetracks within those relevant markets; the impact of higher purses and other incentives in states that compete with our racetracks; costs associated with our efforts in support of alternative gaming initiatives; costs associated with customer relationship management initiatives; a substantial change in law or regulations affecting pari-mutuel and gaming activities; a substantial change in allocation of live racing days; changes in Kentucky, Florida, Illinois or Louisiana law or regulations that impact revenues or costs of racing operations in those states; the presence of wagering and gaming operations at Indiana and other states’ racetracks and casinos near our operations; our continued ability to effectively compete for the country’s horses and trainers necessary to achieve full field horse races; our continued ability to grow our share of the interstate simulcast market and obtain the consents of horsemen’s groups to interstate simulcasting; our ability to execute our acquisition strategy and to complete or successfully operate planned expansion projects; our ability to successfully complete any divestiture transaction; market reaction to our expansion projects; the loss of our totalisator companies or their inability to provide us assurance of the reliability of their internal control processes through Statement on Auditing Standards No. 70 audits or to keep their technology current; the need for various alternative gaming approvals in Florida and Louisiana; our accountability for environmental contamination; the loss of key personnel; the impact of natural and other disasters on our operations and our ability to adjust the casualty losses through our property and business interruption insurance coverage; our ability to integrate Yobet and other businesses we acquire, including our ability to maintain revenues at historic levels and achieve anticipated cost savings; the impact of wagering laws, including changes in laws or enforcement of those laws by regulatory agencies; the outcome of pending or threatened litigation ; changes in our relationships with horsemen’s groups and their memberships; our ability to reach agreement with horsemen’s groups on future purse and other agreements (including, without limiting, agreements on sharing of revenues from gaming and advance deposit wagering); the effect of claims of third parties to intellectual property rights; and the volatility of our stock price.

*You should read this discussion in conjunction with the Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q and the Company’s Annual Report on Form 10-K for the year ended December 31, 2009 for further information, including Part I – Item 1A, “Risk Factors” for a discussion regarding some of the reasons that actual results may be materially different from those we anticipate, as modified by Part II – Item 1A, “Risk Factors” of this Quarterly Report on Form 10-Q.*

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## Table of Contents

### Overview

We are a leading multi-jurisdictional owner and operator of pari-mutuel wagering properties and businesses. Additionally, we offer gaming products through our slot and video poker operations in Louisiana and Florida.

We operate in four operating segments as follows:

1. Racing Operations, which includes:
  - Churchill Downs Racetrack (“Churchill Downs”) in Louisville, Kentucky, an internationally known thoroughbred racing operation and home of the Kentucky Derby since 1875;
  - Arlington Park Race Course (“Arlington Park”), a thoroughbred racing operation in Arlington Heights, Illinois along with ten off-track betting facilities (“OTBs”) in Illinois;
  - Calder Race Course (“Calder”), a thoroughbred racing operation in Miami Gardens, Florida; and
  - Fair Grounds Race Course (“Fair Grounds”), a thoroughbred racing operation in New Orleans, Louisiana along with eleven OTBs in Louisiana.
2. Online Business, which includes:
  - TwinSpire, an Advance Deposit Wagering (“ADW”) business that is licensed as a multi-jurisdictional simulcasting and interactive wagering hub in the state of Oregon;
  - Youbet.com, LLC (“Youbet”), an ADW business acquired by the Company on June 2, 2010 that is licensed as a multi-jurisdictional simulcasting and interactive wagering hub in the state of Oregon;
  - Fair Grounds Account Wagering (“FAW”), an ADW business that is licensed in the state of Louisiana;
  - Bloodstock Research Information Services (“BRIS”), a data service provider for the equine industry; and
  - Our equity investment in HRTV, LLC (“HRTV”) a horseracing television channel.
3. Gaming, which includes:
  - Calder Casino, a slot facility in Florida adjacent to Calder, which opened on January 22, 2010 with over 1,200 slot machines. Additionally, a poker room operation opened within the Calder grandstand on October 23, 2009 under the name “Studz Poker Club”;
  - Fair Grounds Slots, a slot facility in Louisiana adjacent to Fair Grounds which operates over 600 slot machines; and
  - Video Services, Inc. (“VSI”), the owner and operator of more than 800 video poker machines in Louisiana;
4. Other Investments, which includes:
  - United Tote Company and United Tote Canada (collectively “United Tote”), which manufactures and operates pari-mutuel wagering systems for approximately 100 racetracks, OTBs and other pari-mutuel wagering businesses;
  - Churchill Downs Simulcast Productions, LLC (“CDSP”), a provider of television production to the racing industry; and
  - Our other minor investments.

During September 2010, we committed to the dissolution of Churchill Downs Entertainment Group, LLC (“CDE”), which was established in 2009 to conceive and produce large-scale entertainment events. We made the decision to dissolve this group primarily because of our belief that achieving financial success conducting large-scale entertainment events is very difficult in the current economy. As of the date of the filing of this Quarterly Report on Form 10-Q, we do not anticipate further dissolutions of any of our other businesses. The results of operations of CDE have been accounted for as discontinued operations in our Condensed Consolidated Financial Statements included in Item 1 of this Quarterly Report on Form 10-Q. Please refer to further sections of the Management’s Discussion and Analysis of Financial Condition and Results of Operations included in Item 2 as well as our Condensed Consolidated Financial Statements included in Item 1 of this Quarterly Report on Form 10-Q for further details regarding this dissolution.

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## Table of Contents

In order to evaluate the performance of these operating segments internally, we use net revenues and EBITDA as key performance measures of the results of operations. Furthermore, we believe that the use of these measures enables us and investors to evaluate and compare from period to period our operating performance in a meaningful and consistent manner. Because we use EBITDA as a key performance measure of financial performance, we provide a reconciliation of EBITDA to net earnings. However, these measures should not be considered as an alternative to, or more meaningful than, net earnings (as determined in accordance with accounting principles generally accepted in the United States of America) as a measure of our operating results or cash flows (as determined in accordance with accounting principles generally accepted in the United States of America) as a measure of our liquidity.

During the nine months ended September 30, 2010, the continuing overall weakness in the U.S. economy has resulted in considerable negative pressure on discretionary spending. As a result, pari-mutuel wagering and gaming businesses, which are driven, in part, by discretionary spending and industry competition, continued to weaken and, we believe, contributed to a decline in our pari-mutuel handle of 5% during the nine months ended September 30, 2010 compared to the same period of 2009 despite the generation of \$139.5 million of handle by Youbet, which was acquired during June 2010. During the three months ended September 30, 2010, our pari-mutuel handle remained consistent compared to the same period of 2009 but reflected the impact of \$103.7 million of handle generated by Youbet. During the three months ended September 30, 2010, Youbet reported a decline in handle of 14.5%, and during the nine months ended September 30, 2010, Youbet would have reported a decline in handle of 8.0%. On a combined basis, TwinSpires and Youbet handle would have decreased 4.1% and 0.6%, respectively, for the same periods. Total handle on U.S. thoroughbred racing, according to figures published by Equibase, declined 6% during the three months ended September 30, 2010 compared to the same period of 2009 and declined 7% during the nine months ended September 30, 2010 compared to the same period of 2009.

Although there is a growing confidence that global economies, including the U.S. economy, have resumed growth, we believe there remains risk that the recovery will be short-lived, such recovery may not include the industries or markets in which we conduct our business, or that the general economic downturn may resume. We believe there is a strong likelihood that the recent significant economic downturn has had, and for the foreseeable future will continue to have, a negative impact on our financial performance. We believe that, despite uncertain economic conditions, we are in a strong financial position. As of September 30, 2010, there was \$157.6 million of borrowing capacity under our revolving credit facility. To date, we have not experienced any limitations in our ability to access this source of liquidity.

## Recent Developments

### Amendment of Revolving Credit Facility

On November 1, 2010, we entered into Amendment No. 1 to the Second Amended and Restated Credit Agreement (the "Amendment"), which amends certain provisions of the credit agreement and provides for the exercise of the accordion feature whereby the maximum aggregate commitment will be increased from \$275 million to \$375 million. Additionally, the Amendment reduces the pricing schedule for outstanding borrowings by 37.5 basis points and commitment fees by 5 basis points across all leverage pricing levels. The guarantors under the credit agreement continue to be a majority of the Company's wholly-owned subsidiaries. We incurred loan origination costs of approximately \$0.4 million in connection with the Amendment, which will be capitalized and will be amortized as interest expense over the remaining term of the credit agreement. The facility terminates on December 22, 2013.

Generally, borrowings made pursuant to the Amendment will bear interest at a LIBOR-based rate per annum plus an applicable percentage ranging from 1.625% to 3.125% depending on certain of the Company's financial ratios. In addition, under the Amendment, the Company agreed to pay a commitment fee at rates that range from 0.25% to 0.45% of the available aggregate commitment, depending on the Company's leverage ratio.

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## **Table of Contents**

### Acquisition of Harlow's Casino Resort & Hotel

During September 2010, we announced that we entered into a definitive purchase agreement to acquire Harlow's Casino Resort & Hotel in Greenville, Mississippi in a transaction valued at approximately \$138.0 million. We expect to finance the purchase price with borrowings under our revolving credit facility. The transaction is subject to receipt of all required regulatory approvals, including securing a gaming license in Mississippi, obtaining approvals from our lenders under the revolving credit facility and other usual and customary closing conditions. Closing is expected to occur during the fourth quarter of 2010 or first quarter of 2011.

### Dissolution of CDE

During September 2010, we committed to a plan to dissolve CDE, an entity created to develop and produce large-scale entertainment events. We made the decision to dissolve this group primarily because of our belief that achieving financial success conducting large-scale entertainment events is very difficult in the current economy. During the three and nine months ended September 30, 2010, CDE recognized an operating loss of \$7.0 million and \$8.5 million, respectively, which includes \$0.8 million of severance and other benefits costs related to the dissolution of the entity.

### Ohio Legislation

On July 19, 2010, the Ohio Lottery Commission voted unanimously to seek a declaratory judgment that it has the authority to authorize the installation of video lottery terminals at each of Ohio's seven racetracks and promulgated new rules for the operation of video lottery poker machines at racetracks. It is anticipated that video lottery terminals at one or more of Ohio's racetracks may be operational during 2011. We believe that video lottery terminals at Ohio racetracks will provide a competitive advantage to those racetracks and may enable them to increase their purses. Given the proximity of Ohio to Kentucky, the Ohio racetracks may attract horses that would otherwise race at Kentucky racetracks, including Churchill Downs, thus negatively affecting the number of starters and purse size. We believe that fewer starters and lower purses, in turn, may have a negative effect on handle.

### Repayment of Related Party Short-Term Borrowing for Land Acquisition

During 2009, we entered into an agreement with The Duchossois Group ("TDG"), a related party, for the purchase of real estate adjacent to Arlington Park. TDG beneficially owns more than 5% of our common stock. The total purchase price of \$27.5 million was financed by a cash payment of \$3.5 million and a non-interest bearing promissory note of \$24.0 million. During the nine months ended September 30, 2010, we fully repaid the promissory note balance of \$24.0 million in accordance with the original terms of the promissory note.

### Dissolution of TrackNet Media Group LLC Venture

During 2007, together with Magna Entertainment Corporation ("MEC"), we formed a venture, TrackNet Media Group LLC ("TrackNet") through which horseracing content was made readily available through a variety of distribution points and wagering platforms in order to enhance growth within the industry. TrackNet ceased operations during the nine months ended September 30, 2010, and each party will now be responsible for buying and selling its own horseracing content. All existing third-party content agreements involving TrackNet were entered into by TrackNet as an agent for each Company-owned and MEC-owned racetrack. Accordingly, those contracts, and their underlying rights and obligations, will continue to be valid for the remainder of the contracts' respective terms. There was no significant impact on our consolidated financial position or results of operations for the three and nine months ended September 30, 2010 as a result of ceasing operations.

### Receipt of Illinois Riverboat Subsidy

During 2009, we received a payment of \$24.0 million from the Horse Racing Equity Trust Fund ("HRTE Trust Fund") related to subsidies paid by Illinois riverboat casinos in accordance with Public Act 94-804. During the nine months ended September 30, 2010, we received an additional \$14.6 million from the HRTE Trust Fund. The monies have been placed into an escrow account of Arlington Park and are recognized as restricted cash. Revenues from these subsidies continue to be deferred as of September 30, 2010, as challenges regarding the constitutionality of Public Act 94-804 are still being made by the Illinois riverboat casinos.

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## **Table of Contents**

### Youbet.com Merger

On June 2, 2010, we completed our acquisition of Youbet.com, Inc. pursuant to an Agreement and Plan of Merger dated as of November 11, 2009 for an aggregate purchase price of \$131.8 million, which consisted of \$45.3 million in cash and approximately 2.7 million shares of the Company's common stock valued at \$86.5 million based on the closing price of the Company's common stock on June 1, 2010 of \$32.04. The transaction includes the acquisition of the account wagering platform of Youbet and the operations of United Tote, which manufactures and operates pari-mutuel wagering systems for approximately 100 racetracks, OTBs and other pari-mutuel wagering businesses. The primary reason for the merger was to invest in assets with an expected yield on investment and continue our growth in one of the fastest growing segments of the pari-mutuel industry.

### Settlement with ODS

On July 2, 2010, we entered into an agreement with ODS Technologies, LP (d/b/a TVG) ("ODS"), settling a dispute arising under the License and Content Agreement dated as of May 18, 2001, as subsequently amended and modified, between TVG and ODS (the "ODS Agreement"). As part of the settlement, the ODS Agreement was terminated and the Company received a one-time payment of \$1.3 million, which was recognized as miscellaneous income during the three months ended September 30, 2010.

### Impairment of Software

During the second quarter of 2010, we recognized an impairment loss of \$1.3 million associated with software owned by TwinSpires. We determined such software would not be utilized as a result of a reassessment of the use of owned technology in connection with our acquisition of Youbet.

### Income Taxes

We recently underwent federal income tax audits for calendar years 2004 through 2008. During 2005 and 2006, we received approximately \$23.5 million of proceeds related to the sale of Personal Seat Licenses ("PSLs") sold in connection with the renovation of Churchill Downs. The PSLs that were sold included those with terms of 30 years and 5 years and provided the purchaser the right to purchase tickets to the Kentucky Derby, Kentucky Oaks and Breeders' Cup races each year during the term of the license. Accordingly, for tax purposes, we deferred the income for the personal seat licenses over the respective terms of the licenses.

During 2009, the Internal Revenue Service (the "IRS") proposed that the income related to the sale of the PSLs is taxable during the period we received the proceeds (the "Proposed Audit Adjustment"). As a result, the Proposed Audit Adjustment served to increase the amount of the income taxes due for each of the years 2005 and 2006.

On April 14, 2010, we defended our position of deferring income related to the sale of PSLs using a fast track mediation process offered by the IRS. During the fast track mediation process, we agreed to change our method of accounting for proceeds related to the sale of PSLs to the deferral method provided for in Revenue Procedure 2004-34, effective for the taxable year ended December 31, 2007. As a result, our taxable income for each of the years ended December 31, 2007 and 2008 will increase by \$19.1 million and \$0.4 million, respectively. In accordance with the settlement entered into during the fast track mediation process, we recognized an income tax benefit from continuing operations of \$1.6 million during the nine months ended September 30, 2010 reflecting a reduction of interest expense previously estimated and recognized during 2009 as a result of the Proposed Audit Adjustment.

## **Legislative and Regulatory Changes**

### Federal

On October 13, 2006, President George W. Bush signed into law The Unlawful Internet Gambling Enforcement Act of 2006 (the "UIGEA"). The UIGEA prohibits those involved in the business of betting or wagering from accepting any financial instrument, electronic or otherwise, for deposit that is intended to be utilized for unlawful Internet gambling. The UIGEA declares that nothing in the act may be construed to prohibit any activity allowed by the federal Interstate Horseracing Act of 1978 (the "IHA"). The UIGEA also contains a "Sense of Congress," which explicitly states that it is not intended to criminalize any activity currently permitted by federal law. The Secretary of the Treasury was directed to promulgate regulations to enforce the provisions of the UIGEA within 270 days. The Secretary was further directed to ensure the

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## Table of Contents

regulations do not prohibit any activity which is excluded from the definition of unlawful Internet gambling, including those activities legal under the IHA. On November 12, 2008, the Department of Treasury and the Federal Reserve Board issued final rules and regulations to implement the UIGEA which required compliance by December 1, 2009.

On November 28, 2009, the effective date of the UIGEA regulations was delayed until June 1, 2010. We worked diligently with the National Thoroughbred Racing Association and other interested parties including Visa, MasterCard, and the banking industry, to distinguish ADW businesses from unlawful internet gaming. In preparation for the June 1, 2010 deadline, Visa and MasterCard issued separate bulletins that provided a framework for legal internet gambling transactions. Consistent with the intent of the UIGEA regulations, the legal internet gaming exception included horseracing, lottery, and dog racing transactions. TwinSpires was able to meet the stringent requirements for legal internet gambling certifications by both MasterCard and Visa by the June 1, 2010 deadline. Subsequent to the closing of the Youbet acquisition, we began working to harmonize the certifications for Youbet and TwinSpires, and we are continuing to work with MasterCard, Visa and the banking industry to minimize the impact of UIGEA on our ADW businesses. Although TwinSpires and Youbet have been approved to offer internet gambling transactions under UIGEA by multiple credit card companies and financial institutions, the willingness of issuing banks to accept these transactions is uncertain. We believe that issuing banks' unwillingness to accept these transactions could have a material, adverse impact on our business, financial condition and results of operations.

### Florida

During 2010, the Florida legislature passed Senate Bill 622 ("SB 622"), which contained a new Tribal Compact. A provision of SB 622 made Chapter 2009-170, Laws of Florida, effective on July 1, 2010. As a result, the annual license fee was reduced to \$2.5 million on July 1, 2010, and an additional reduction to \$2.0 million was established that will be due July 1, 2011. Pursuant to the new Tribal Compact, which was approved by the Florida legislature and the Governor of Florida, the Seminole tribe gained the exclusive right to have blackjack and other table games at three Broward County casinos and two other casinos in Immokalee and Tampa. All seven tribal casinos are able to continue operating Las Vegas-style slot machines. Other portions of Chapter 2009-170, Laws of Florida, purport to permit the operation of slot machines at quarter horse facilities in Miami-Dade County. In particular, Section 19, Chapter 2009-170, Laws of Florida, purports to permit Hialeah Race Course, located approximately 12 miles from Calder, to open as a quarter horse facility and operate slot machines after two consecutive years of quarter horseracing. On June 18, 2010, Calder filed a constitutional challenge as to the provisions of Section 19 of Chapter 2009-170, Laws of Florida, alleging that Section 19 violates Article X, Section 23, of the Florida Constitution, is a prohibited act of the Florida legislature and expands the limits set in the constitution for slot machine licenses. The suit is pending in Leon County, Florida.

On July 21, 2010, the Florida Quarter Horse Track Association, Inc. filed a suit against the state of Florida, Department of Business and Professional Regulation, Division of Pari-Mutuel Wagering, Calder Race Course, Inc. and Tropical Park, Inc. ("Tropical Park"), alleging that the Florida statute authorizing the issuance of the original thoroughbred racing permit to Calder in 1969 was an unconstitutional special law under the Florida constitution and the arrangement between Tropical Park and Calder under which Tropical Park conducts its race meets at Calder is not authorized by the Florida statute. The case is pending in Leon County, Florida.

### Kentucky

The 2010 session of the Kentucky legislature concluded on April 15, 2010, and several bills impacting gaming in Kentucky were filed. A bill was filed in the Kentucky Senate requiring a constitutional amendment to approve expanded gaming in any form and was defeated on the Senate floor. An additional bill was filed in the Kentucky Senate that would have allowed gaming in counties that conduct thoroughbred racing, with a portion of the proceeds going to purses. The bill would have required both a statewide and local referendum to be effective and would not have reserved any license for Kentucky racetracks. In the House, the Speaker filed a bill permitting video lottery terminals at Kentucky racetracks which was substantially similar to the bills filed in both the regular and special sessions of 2009. House Bill 368 was filed which would have placed an excise tax on ADW wagers made by Kentucky residents. None of these bills became law.

On July 20, 2010, the Kentucky Horseracing Commission (the "KHRC") approved a change in state regulations that would allow racetracks to offer pari-mutuel "Historical Racing" machines ("HRM"). HRMs base their payouts on the results of previously-run races at racetracks across North America. Portions of previously-run-races, the length of which is chosen by the player, can be viewed, and winning combinations are presented via video terminals that convert the corresponding wager to "slot like" games. Despite the positive vote from the KHRC, there are questions with regard to the viability of the HRMs in a competitive wagering market such as Louisville and the legality of regulations enacted. No decisions will be made on whether to pursue HRMs until both of these questions are answered. A declaratory judgment has been filed in Franklin Circuit Court on behalf of the Commonwealth of Kentucky and all Kentucky racetracks to ensure proper legal authority. Currently, only Oaklawn Park Racetrack and Southland Greyhound Park, both in Arkansas, offer the HRMs.

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## Table of Contents

### Illinois

#### *Illinois Senate Bill 3146*

The state of Illinois is facing a budget shortfall, and legislation supported by Illinois horsemen and racetracks, Senate Bill 3146 (“SB 3146”), would allow electronic gaming at the six Illinois racetracks. This plan could generate up to \$400 million in one-time licensing fees and annual tax revenues between \$150 million and \$300 million for the state of Illinois.

SB 3146 would authorize Arlington Park to operate up to 1,200 gaming positions (slots or video poker) for a license fee of \$25,000 per position. SB 3146 would also authorize Quad City Downs, owned by Arlington Park, to operate up to 900 gaming positions (slots or video poker) at an initial licensing fee of \$12,500 per position. Gaming taxes would be established at the same rate as riverboat casinos, which currently is a graduated rate that varies from 15% of gross gaming revenues to 50% of gross gaming revenues depending on the level of gross gaming revenues. The next opportunity for passage of SB 3146 will be during the Fall Veto Session of the Illinois legislature, which will be held from November 16 through December 1, 2010.

#### *Horse Racing Equity Trust Fund*

During 2006, the Illinois General Assembly enacted Public Act 94-804, which created the HRE Trust Fund which is funded by a 3% “surcharge” on revenues of Illinois riverboat casinos that meet a certain revenue threshold. Approximately 60% of the funds are to be used for horsemen’s purses (57% for thoroughbred meets and 43% for standardbred meets). The remaining 40% of monies paid to the HRE Trust Fund are to be distributed to Illinois organizational licensees, pursuant to percentage allocations set forth in Public Act 94-804, for the purpose of improving, maintaining, marketing and operating their racetracks.

During November 2008, the Illinois General Assembly passed Public Act 95-1008 to extend Public Act 94-804 for a period of three years beginning December 12, 2008. The riverboat casinos have paid all monies required under Public Act 95-1008 into a special protest fund account, which the trial court has retained via a preliminary injunction. The riverboat casinos moved to stay dissolution of the injunction pending their appeal of the trial court’s dismissal order. The trial court denied the stay, as did the Appellate Court of Illinois on April 8, 2010. During the three months ended September 30, 2010, we received \$14.6 million from the HRE Trust Fund, which is currently being held in an escrow account held by Arlington Park. Of the total monies we received, we anticipate \$6.1 million will be retained by Arlington Park and \$8.5 million will be paid into Arlington Park’s purse account. Arlington Park filed an administrative appeal in the Circuit Court of Cook County on August 18, 2009 (*Arlington Park Racecourse LLC v. Illinois Racing Board*, 09 CH 28774), challenging the Illinois Racing Board’s (“IRB”) allocation of funds paid to organization licensees out of the HRE Trust Fund based upon handle generated by certain ineligible licensees, as contrary to the language of the statute. Defendant Hawthorne Racecourse LLC moved for dismissal of the administrative appeal while challenging subject matter jurisdiction and this challenge was rejected by the Circuit Court on April 16, 2010. Briefing on Arlington’s administrative appeal was completed in July 2010, and oral argument proceeded on October 19, 2010. The Court set the date of November 10, 2010 to rule on Arlington Park’s administrative appeal. Hawthorne Racecourse filed a separate administrative appeal on June 11, 2010 (*Hawthorne Racecourse, Inc. v. Illinois Racing Board et. al.*, Case No. 10 CH 24439), challenging the IRB’s unwillingness to hold another meeting in 2010 to reconstrue the statutory language in Public Act 94-1008 which the IRB had already construed in making its July 14, 2009 decision. The IRB and Arlington Park have moved to dismiss Hawthorne’s appeal on subject matter jurisdiction grounds. The motions have been fully briefed and oral argument on the motions to dismiss Hawthorne’s separate appeal is set for December 8, 2010. The monies received by Arlington Park are subject to a federal court injunction and thus remain in escrow pending the appeal of the federal lawsuit.

#### *Other Items*

On July 12, 2010, the IRB issued Rule 325.60, which limits the amount of host fees paid by ADW businesses to racetracks outside of Illinois to 5% of handle. On August 31, 2010, the IRB amended Rule 325.60 to set the maximum host fees paid by ADW businesses to racetracks outside of Illinois to 9% of handle. From July 12, to September 1, 2010 TwinSpires and Yobet did not offer certain racetracks’ content to Illinois residents through their wagering platforms. TwinSpires and Yobet are currently offering all their racetracks’ content to Illinois residents.

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## **Table of Contents**

### Louisiana

A resolution calling for a study of the horseracing industry, Senate Concurrent Resolution 130, sponsored by Senator Nick Gautreaux, passed the Louisiana Senate. The resolution urges and requests a joint committee of the Senate and House to meet during the interim “to study and determine whether the Louisiana State Racing Commission is properly regulating the horse racing industry in Louisiana, whether the commission is meeting the stated legislative intent, policy, and purposes as prescribed by Louisiana law, and whether the commission is utilizing the best practices in performing its function.” The resolution mandates that the joint committee submit a written report of its findings to the legislature prior to March 1, 2011.

### California

On September 23, 2010, the governor of California signed a bill that approved exchange betting on horseracing by California residents and on California racetracks. The bill does not allow exchange wagering before May 2012 but makes California the first state to approve this type of wagering. Exchange wagering strays from pari-mutuel wagering in that it allows customers to propose their own odds on certain types of wagers on horseracing, which may be accepted by a second customer. Exchange wagering may have a negative impact on our current pari-mutuel operations, including our ADW business. Furthermore, California’s approval of exchange wagering may set a precedent for other states to approve exchange wagering, creating additional risk of a negative impact on our pari-mutuel wagering business.

## Table of Contents

### RESULTS OF CONTINUING OPERATIONS

#### Pari-mutuel Handle by Segment

The following table sets forth, for the periods indicated, pari-mutuel financial handle data by our reported segments (in thousands):

|                           | Three Months Ended<br>September 30, |             | Change      |      | Nine Months Ended<br>September 30, |             | Change       |      |
|---------------------------|-------------------------------------|-------------|-------------|------|------------------------------------|-------------|--------------|------|
|                           | 2010                                | 2009        | \$          | %    | 2010                               | 2009        | \$           | %    |
| <b>Racing Operations:</b> |                                     |             |             |      |                                    |             |              |      |
| <b>Churchill Downs</b>    |                                     |             |             |      |                                    |             |              |      |
| Total handle              | \$ 40,801                           | \$ 42,505   | \$ (1,704)  | -4%  | \$ 487,146                         | \$ 504,011  | \$ (16,865)  | -3%  |
| Net pari-mutuel revenues  | \$ 3,557                            | \$ 3,702    | \$ (145)    | -4%  | \$ 39,471                          | \$ 41,130   | \$ (1,659)   | -4%  |
| Commission %              | 8.7%                                | 8.7%        |             |      | 8.1%                               | 8.2%        |              |      |
| <b>Arlington Park</b>     |                                     |             |             |      |                                    |             |              |      |
| Total handle              | \$251,062                           | \$341,383   | \$ (90,321) | -26% | \$ 528,758                         | \$ 686,777  | \$ (158,019) | -23% |
| Net pari-mutuel revenues  | \$ 24,359                           | \$ 29,369   | \$ (5,010)  | -17% | \$ 53,484                          | \$ 67,403   | \$ (13,919)  | -21% |
| Commission %              | 9.7%                                | 8.6%        |             |      | 10.1%                              | 9.8%        |              |      |
| <b>Calder</b>             |                                     |             |             |      |                                    |             |              |      |
| Total handle              | \$200,276                           | \$217,006   | \$ (16,730) | -8%  | \$ 394,803                         | \$ 442,389  | \$ (47,586)  | -11% |
| Net pari-mutuel revenues  | \$ 20,703                           | \$ 21,940   | \$ (1,237)  | -6%  | \$ 39,731                          | \$ 42,935   | \$ (3,204)   | -7%  |
| Commission %              | 10.3%                               | 10.1%       |             |      | 10.1%                              | 9.7%        |              |      |
| <b>Fair Grounds</b>       |                                     |             |             |      |                                    |             |              |      |
| Total handle              | \$ 28,420                           | \$ 32,186   | \$ (3,766)  | -12% | \$ 262,415                         | \$ 320,361  | \$ (57,946)  | -18% |
| Net pari-mutuel revenues  | \$ 5,032                            | \$ 5,504    | \$ (472)    | -9%  | \$ 25,057                          | \$ 27,914   | \$ (2,857)   | -10% |
| Commission %              | 17.7%                               | 17.1%       |             |      | 9.5%                               | 8.7%        |              |      |
| <b>Online Business</b>    |                                     |             |             |      |                                    |             |              |      |
| Total handle              | \$193,415                           | \$ 80,427   | \$112,988   | F    | \$ 421,037                         | \$ 255,531  | \$ 165,506   | 65%  |
| Net pari-mutuel revenues  | \$ 36,820                           | \$ 15,844   | \$ 20,976   | F    | \$ 81,169                          | \$ 49,823   | \$ 31,346    | 63%  |
| Commission %              | 19.0%                               | 19.7%       |             |      | 19.3%                              | 19.5%       |              |      |
| <b>Eliminations</b>       |                                     |             |             |      |                                    |             |              |      |
| Total handle              | \$ (22,808)                         | \$ (21,498) | \$ (1,310)  | -6%  | \$ (78,418)                        | \$ (77,651) | \$ (767)     | -1%  |
| Net pari-mutuel revenues  | \$ (2,130)                          | \$ (1,425)  | \$ (705)    | -49% | \$ (6,931)                         | \$ (5,409)  | \$ (1,522)   | -28% |
| <b>Total</b>              |                                     |             |             |      |                                    |             |              |      |
| Handle                    | \$691,166                           | \$692,009   | \$ (843)    | —    | \$2,015,741                        | \$2,131,418 | \$ (115,677) | -5%  |
| Net pari-mutuel revenues  | \$ 88,341                           | \$ 74,934   | \$ 13,407   | 18%  | \$ 231,981                         | \$ 223,796  | \$ 8,185     | 4%   |
| Commission %              | 12.8%                               | 10.8%       |             |      | 11.5%                              | 10.5%       |              |      |

NM: Not meaningful

U: > 100% unfavorable      F: >100% favorable

## Table of Contents

### Three Months Ended September 30, 2010 Compared to Three Months Ended September 30, 2009

The following table sets forth, for the periods indicated, certain operating data for our properties (in thousands, except per common share data and live race days):

|   | Three Months Ended<br>September 30, |                  | Change          |     |
|---|-------------------------------------|------------------|-----------------|-----|
|   | 2010                                | 2009             | \$              | %   |
| Number of thoroughbred live race days                               | 111                                 | 118              | (7)             | -6% |
| Net pari-mutuel revenues  | \$ 88,341                           | \$ 74,934        | \$13,407        | 18% |
| Gaming revenues   | 27,152                              | 13,841           | 13,311          | 96% |
| Other operating revenues  | 20,251                              | 12,121           | 8,130           | 67% |
| Total net revenues from continuing operations                       | <u>\$135,744</u>                    | <u>\$100,896</u> | <u>\$34,848</u> | 35% |
| Operating income  | \$ 3,295                            | \$ 2,460         | \$ 835          | 34% |
| Operating income margin   | 2%                                  | 2%               |                 |     |
| Earnings (loss) from continuing operations                          | \$ 3,700                            | \$ (1,216)       | \$ 4,916        | F   |
| Diluted earnings (loss) from continuing operations per common share | \$ 0.22                             | \$ (0.09)        |                 |     |

Our total net revenues increased \$34.8 million primarily due to the addition of Youbet, which contributed \$19.1 million in net pari-mutuel revenues during the three months ended September 30, 2010. Gaming revenues increased as we opened Calder Casino on January 22, 2010, which generated gaming revenues of \$12.2 million during the three months ended September 30, 2010. Other operating revenues increased \$8.1 million primarily due to the addition of United Tote, which contributed \$5.7 million of revenues during the three months ended September 30, 2010. Partially offsetting these increases was a decline in net pari-mutuel revenues within the Racing Operations segment of \$6.9 million during the three months ended September 30, 2010. Arlington Park pari-mutuel revenues, particularly those related to export wagering, decreased due to eight fewer race days conducted during the three months ended September 30, 2010 compared to the same period of the prior year. In addition, we believe competitive pressures, including those resulting from New Jersey gaming-subsidized purses contributed to fuller fields at Monmouth Park and less wagering on Arlington Park and Calder racing content. Further discussion of net revenue variances by our reported segments is detailed below.

### Consolidated Operating Expenses

The following table is a summary of our consolidated operating and SG&A expenses (in thousands):

|                               | Three Months Ended<br>September 30, |                 | Change          |      |
|-------------------------------|-------------------------------------|-----------------|-----------------|------|
|                               | 2010                                | 2009            | \$              | %    |
| Purse expenses                | \$ 26,357                           | \$29,336        | \$ (2,979)      | -10% |
| Depreciation and amortization | 12,394                              | 7,523           | 4,871           | 65%  |
| Other operating expenses      | 78,417                              | 48,485          | 29,932          | 62%  |
| SG&A expenses                 | 15,281                              | 13,092          | 2,189           | 17%  |
| Total                         | <u>\$132,449</u>                    | <u>\$98,436</u> | <u>\$34,013</u> | 35%  |
| Percent of revenue            | 98%                                 | 98%             |                 |      |

Significant items affecting comparability of consolidated operating expenses include:

- Other operating expenses increased primarily due to expenses of \$18.2 million incurred by Youbet and United Tote during the three months ended September 30, 2010, which includes simulcasting and tote expenses of \$11.0 million and employee-related costs of \$4.5 million. In addition, we incurred \$7.0 million related to the operation of Calder Casino, which opened during January 2010. These costs include promotional expenditures of \$2.8 million,

## Table of Contents

employee-related costs of \$2.1 million and \$1.0 million of rent expense for slot machines. Finally, we were unfavorably impacted by a prior year insurance recovery of \$2.5 million within our Racing Operations at Calder and a prior year real estate tax refund of \$2.4 million at Arlington Park during the three months ended September 30, 2009.

- Depreciation and amortization expense increased \$4.9 million, primarily reflecting \$2.8 million related to capital expenditures incurred for the construction of Calder Casino. Additionally, we incurred depreciation and amortization expense of \$2.4 million related to the operation of Youbet and United Tote during the three months ended September 30, 2010.
- SG&A expenses increased primarily due to employee-related costs of \$3.5 million at Calder Casino, Youbet and United Tote during the three months ended September 30, 2010. Such costs include \$1.7 million of one-time charges related to our reorganization of Youbet. Partially offsetting this increase was lower legal expenses of \$0.6 million as we incurred costs related to the bankruptcy filing of Magna Entertainment Corporation (“MEC”) and the Illinois riverboat subsidy during the three months ended September 30, 2009. Additionally, we incurred \$0.5 million of lower employee-related costs at corporate for the three months ended September 30, 2010.
- Purse expenses decreased \$5.1 million within the Racing Operations segment primarily as a result of lower pari-mutuel revenues as well as a \$1.5 million purse supplement made in the prior year to the Kentucky Horsemen’s Benevolent and Protective Association (“KHBPA”). These declines were partially offset by \$2.0 million of purse expense generated by Calder Casino during the three months ended September 30, 2010.

### Other Income (Expense) and Income Tax Provision

The following table is a summary of our other income (expense) and income tax provision (in thousands):

|  | Three Months Ended<br>September 30, |                | Change          |      |
|--|-------------------------------------|----------------|-----------------|------|
|  | 2010                                | 2009           | \$              | %    |
| Interest income                              | \$ 30                               | \$ 393         | \$ (363)        | -92% |
| Interest expense                             | (1,625)                             | (245)          | (1,380)         | U    |
| Equity in loss of unconsolidated investments | (470)                               | (568)          | 98              | 17%  |
| Miscellaneous, net                           | 1,832                               | 322            | 1,510           | F    |
| Other income (expense)                       | <u>\$ (233)</u>                     | <u>\$ (98)</u> | <u>\$ (135)</u> | U    |
| Income tax provision                         | \$ 638                              | \$(3,578)      | \$ 4,216        | 118% |
| Effective tax rate                           | -21%                                | 151%           |                 |      |

Significant items affecting the comparability of other income and expense and income tax provision include:

- Interest expense increased during the three months ended September 30, 2010 primarily as a result of higher average outstanding debt balances under our revolving credit facility required for the acquisition of Youbet and capital expenditures incurred at Calder Casino.
- Interest income decreased during the three months September 30, 2010 as a result of lower average cash balances due to borrowings made to finance the construction of Calder Casino and the acquisition of Youbet.
- Miscellaneous income increased during the three months ended September 30, 2010 primarily due to the recognition of income related to a settlement with ODS. As part of the settlement, a simulcast service agreement was terminated, and the Company received a one-time payment of \$1.3 million.
- The effective tax rate for the three months ended September 30, 2010 was affected by the recognition of approximately \$1.0 million of income tax benefits recorded during the third quarter of 2010 primarily related to the adjustment of permanent differences to reflect positions taken on federal income tax returns. Additionally, during the three months ended September 30, 2009, we recognized \$2.3 million of income tax expense related to the Proposed Audit Adjustment of prior year income tax returns by the IRS.

## Table of Contents

### Net Revenues By Segment

The following table presents net revenues, including intercompany revenues, by our reported segments (in thousands):

|                         | Three Months Ended<br>September 30, |                  | Change          |      |
|-------------------------|-------------------------------------|------------------|-----------------|------|
|                         | 2010                                | 2009             | \$              | %    |
| Churchill Downs         | \$ 5,785                            | \$ 5,459         | \$ 326          | 6%   |
| Arlington Park          | 30,644                              | 34,735           | (4,091)         | -12% |
| Calder                  | 22,161                              | 23,044           | (883)           | -4%  |
| Fair Grounds            | 5,981                               | 6,545            | (564)           | -9%  |
| Total Racing Operations | \$ 64,571                           | \$ 69,783        | \$ (5,212)      | -7%  |
| Online Business         | 38,851                              | 17,536           | 21,315          | F    |
| Gaming                  | 28,306                              | 14,104           | 14,202          | F    |
| Other Investments       | 6,824                               | 1,349            | 5,475           | F    |
| Corporate Revenues      | 64                                  | 85               | (21)            | -25% |
| Eliminations            | (2,872)                             | (1,961)          | (911)           | -46% |
| Net Revenues            | <u>\$135,744</u>                    | <u>\$100,896</u> | <u>\$34,848</u> | 35%  |

Significant items affecting comparability of our revenues by segment include:

- Online Business revenues increased \$21.3 million primarily due to the addition of Yobet revenues of \$19.5 million during the quarter ended September 30, 2010. In addition, net revenues increased \$1.8 million, or 10%, at TwinSpires and FAW, which experienced 12% higher wagering during the three months ended September 30, 2010 compared to the same period of the prior year. We believe this increase was in part due to higher wagering on Monmouth Park driven by New Jersey gaming-subsidized purses, which contributed to fuller fields.
- Gaming segment revenues increased primarily as a result of the commencement of operations of Calder Casino, which operates over 1,200 slot machines, during 2010. During the three months ended September 30, 2010, Calder Casino recognized total net revenues of \$13.2 million. The Fair Grounds slot facility reported total net revenues of \$8.6 million during the three months ended September 30, 2010, which was \$0.6 million higher than total net revenues recognized during the same period of the prior year.  
During the three months ended September 30, 2010, gross gaming revenues of the Fair Grounds slot facility, which is calculated as gross gaming revenues before taxes and promotional deductions but after customer payouts, were \$10.5 million, which was comparable to gross gaming revenues of the same period of the prior year. Gross win per unit at Fair Grounds was \$190 per machine per day during the three months ended September 30, 2010 compared to \$180 per machine per day during the same period of 2009. Calder Casino gross gaming revenues were \$17.9 million, and gross win per unit was \$161 per machine per day during the three months ended September 30, 2010.
- Other Investments' revenues increased \$5.5 million primarily due to the addition of United Tote revenues of \$5.7 million during the quarter ended September 30, 2010.
- Racing Operations revenues decreased \$5.2 million primarily due to a decline in pari-mutuel revenues at Arlington Park as we conducted eight fewer race days there. Additionally, we believe Arlington Park and Calder revenues, particularly those related to export wagering, declined due to competitive pressures, including those resulting from New Jersey gaming-subsidized purses at Monmouth Park.

## Table of Contents

### Segment EBITDA

The following table presents EBITDA by our reported segments (in thousands):

|                   | Three Months Ended<br>September 30, |                 | Change          |      |
|-------------------|-------------------------------------|-----------------|-----------------|------|
|                   | 2010                                | 2009            | \$              | %    |
| Racing Operations | \$ 1,254                            | \$ 3,428        | \$(2,174)       | -63% |
| Online Business   | 5,818                               | 2,802           | 3,016           | F    |
| Gaming            | 7,892                               | 3,884           | 4,008           | F    |
| Other Investments | 1,792                               | 831             | 961             | F    |
| Corporate         | 296                                 | (1,208)         | 1,504           | F    |
| Total EBITDA      | <u>\$17,052</u>                     | <u>\$ 9,737</u> | <u>\$ 7,315</u> | 75%  |

Refer to Note 10 of the Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q for further information about our reported segments, including a reconciliation of EBITDA to earnings from continuing operations.

Significant items affecting comparability of our EBITDA by segment include:

- Gaming EBITDA increased \$4.0 million primarily reflecting \$2.4 million of positive EBITDA generated by Calder Casino during the three months ended September 30, 2010 compared to an EBITDA loss of \$0.4 million related to preopening expenses incurred during the three months ended September 30, 2009. EBITDA at the Fair Grounds slot facility was \$2.7 million during the three months ended September 30, 2010 and improved \$0.6 million over the same period of the prior year driven primarily by higher gaming revenues. VSI EBITDA increased \$0.6 million to \$2.8 million, which was due, in part, to the operating performance of an OTB that opened during the fourth quarter of 2009.
- Online Business EBITDA increased \$3.0 million primarily due to \$1.6 million of positive EBITDA contributed by Yobet during the three months ended September 30, 2010, which included \$1.7 million of one-time charges related to the reorganization of Yobet. Yobet's EBITDA for the three months ended September 30, 2010 included allocated corporate overhead of \$0.7 million. In addition, TwinSpires and FAW EBITDA increased \$1.4 million in part due to higher wagering on Monmouth Park that we believe was driven by New Jersey gaming-subsidized purses, which contributed to fuller fields.
- Corporate EBITDA increased primarily due to the effect of a favorable settlement with ODS, which contributed \$1.3 million during the quarter ended September 30, 2010.
- Other Investments EBITDA increased primarily due to the contribution of \$1.2 million of positive EBITDA by United Tote during the three months ended September 30, 2010.
- Racing Operations EBITDA decreased \$2.2 million and was primarily driven by \$2.5 million in insurance recoveries recognized at Calder and \$2.4 million of real estate tax refunds at Arlington Park during the three months ended September 30, 2009. Partially offsetting these decreases was a decrease in purse expense of \$1.5 million from a purse supplement made to the KHBPA during the three months ended September 30, 2009 by Churchill Downs. We experienced a decline in Racing Operations EBITDA of \$1.0 million related to the deterioration in pari-mutuel business that we believe was caused by a shift in wagering to Monmouth Park as previously mentioned. Lower corporate overhead of \$2.2 million was allocated to the Racing Operations during the three months ended September 30, 2010 compared to the same period of the prior year and partially offset these declines.

## Table of Contents

### Discontinued Operations

The following table presents losses from discontinued operations, which includes the results of operations of CDE, Hollywood Park and Ellis Park for the three months ended September 30, 2010 and 2009 (in thousands):

|   | Three Months Ended<br>September 30, |                   | Change            |    |
|---|-------------------------------------|-------------------|-------------------|----|
|   | 2010                                | 2009              | \$                | %  |
| Net revenues  | \$ 6,303                            | \$ —              | \$ 6,303          | NM |
| Operating expenses  | 11,921                              | —                 | 11,921            | NM |
| Selling, general and administrative expenses              | 1,389                               | —                 | 1,389             | NM |
| Operating loss  | (7,007)                             | —                 | (7,007)           | U  |
| Other income (expense):                                   |                                     |                   |                   |    |
| Miscellaneous, net  | —                                   | (46)              | 46                | F  |
|   | —                                   | (46)              | 46                | F  |
| Loss from continuing operations before income tax benefit | (7,007)                             | (46)              | (6,961)           | U  |
| Income tax benefit (provision)                            | 2,618                               | (1,063)           | 3,681             | F  |
| Net loss  | <u>\$ (4,389)</u>                   | <u>\$ (1,109)</u> | <u>\$ (3,280)</u> | U  |

## Table of Contents

### Nine Months Ended September 30, 2010 Compared to Nine Months Ended September 30, 2009

The following table sets forth, for the periods indicated, certain operating data for our properties (in thousands, except per common share data and live race days):

|  | Nine Months Ended<br>September 30, |                  | Change          |      |
|--|------------------------------------|------------------|-----------------|------|
|  | 2010                               | 2009             | \$              | %    |
| Number of thoroughbred live race days                        | 278                                | 297              | (19)            | -6%  |
| Net pari-mutuel revenues                                     | \$231,981                          | \$223,796        | \$ 8,185        | 4%   |
| Gaming revenues  | 79,213                             | 46,493           | 32,720          | 70%  |
| Other operating revenues                                     | 100,112                            | 84,381           | 15,731          | 19%  |
| Total net revenues from continuing operations                | <u>\$411,306</u>                   | <u>\$354,670</u> | <u>\$56,636</u> | 16%  |
| Operating income   | \$ 35,836                          | \$ 44,587        | \$(8,751)       | -20% |
| Operating income margin                                      | 9%                                 | 13%              |                 |      |
| Earnings from continuing operations                          | \$ 23,825                          | \$ 24,573        | \$ (748)        | -3%  |
| Diluted earnings from continuing operations per common share | \$ 1.56                            | \$ 1.75          |                 |      |

Our total net revenues increased \$56.6 million primarily as a result of the operation of Calder Casino, which opened on January 22, 2010 and generated gaming revenues of \$32.1 million during the nine months ended September 30, 2010. In addition, net revenues increased due to the addition of Yobet and United Tote of \$34.0 million for its four months of operation during the nine months ended September 30, 2010. Pari-mutuel revenues generated by the continuing growth of TwinSpires and FAW increased \$5.7 million during the nine months ended September 30, 2010. These increases in net revenues were offset by a decline in Racing Operations revenues driven primarily by the fact that we conducted nineteen fewer live race days during the first nine months of 2010 compared to the same period of 2009. Further discussion of net revenue variances by our reported segments is detailed below.

### Consolidated Operating Expenses

The following table is a summary of our consolidated operating and SG&A expenses (in thousands):

|                               | Nine Months Ended<br>September 30, |                  | Change          |      |
|-------------------------------|------------------------------------|------------------|-----------------|------|
|                               | 2010                               | 2009             | \$              | %    |
| Purse expenses                | \$ 81,664                          | \$ 90,736        | \$(9,072)       | -10% |
| Depreciation and amortization | 34,409                             | 22,399           | 12,010          | 54%  |
| Other operating expenses      | 215,460                            | 159,421          | 56,039          | 35%  |
| SG&A expenses                 | 43,937                             | 37,527           | 6,410           | 17%  |
| Total                         | <u>\$375,470</u>                   | <u>\$310,083</u> | <u>\$65,387</u> | 21%  |
| Percent of revenue            | 91%                                | 87%              |                 |      |

Significant items affecting comparability of consolidated operating expenses include:

- Other operating expenses increased \$56.0 million primarily due to the recognition of \$24.6 million of expenses related to the four months of operation of Yobet and United Tote, which include expenditures incurred to acquire racing content. In addition, we incurred \$23.9 million related to the operation of Calder Casino, which includes promotional expenditures of \$10.5 million, employee-related costs of \$6.4 million and \$3.2 million of rent expense for slot machines. Finally, we experienced increased expenses related to acquiring racing content within TwinSpires and FAW of \$4.0 million as a result of regulations passed in several states during late 2009.

## Table of Contents

- Depreciation and amortization expense increased \$12.0 million, primarily reflecting \$9.0 million related to capital expenditures incurred to construct Calder Casino. Additionally, we incurred \$3.3 million in depreciation and amortization expense related to Youbet and United Tote during its four months of operations during the nine months ended September 30, 2010.
- SG&A expenses increased \$6.4 million primarily due to \$3.1 million of expenses incurred that were associated with our acquisition of Youbet. Additionally, we incurred an increase in employee-related costs of \$2.3 million at Calder Casino and \$3.5 million at Youbet and United Tote. Such costs include \$2.1 million of one-time charges related to the reorganization of Youbet. Partially offsetting this increase was lower legal expenses of \$0.5 million as we incurred costs related to the bankruptcy filings of MEC and the Illinois riverboat subsidy during the nine months ended September 30, 2009. Finally, there was a decrease of \$1.2 million of compensation expense related to our equity compensation and long-term incentive plans for the nine months ended September 30, 2010 compared to the same period of 2009.
- Purse expenses decreased \$9.1 million primarily as a result of a decline of \$10.8 million within Racing Operations caused by lower pari-mutuel revenues for the nine months ended September 30, 2010. In addition, purse expense further decreased by \$2.1 million due to \$4.3 million of source market fees recognized at Arlington Park during the nine months ended September 30, 2009. Partially offsetting this decline was \$4.0 million of purse expense generated by Calder Casino during the nine months ended September 30, 2010

### Other Income (Expense) and Income Tax Provision

The following table is a summary of our other income (expense) and income tax provision (in thousands):

|  | Nine Months Ended |               | Change            |      |
|--|-------------------|---------------|-------------------|------|
|  | 2010              | 2009          | \$                | %    |
| Interest income                              | \$ 158            | \$ 780        | \$ (622)          | -80% |
| Interest expense                             | (4,303)           | (772)         | (3,531)           | U    |
| Equity in loss of unconsolidated investments | (317)             | (641)         | 324               | 51%  |
| Miscellaneous, net                           | 2,485             | 1,042         | 1,443             | F    |
| Other (expense) income                       | <u>\$ (1,977)</u> | <u>\$ 409</u> | <u>\$ (2,386)</u> | U    |
| Income tax provision                         | \$(10,034)        | \$(20,423)    | \$10,389          | 51%  |
| Effective tax rate                           | 30%               | 45%           |                   |      |

Significant items affecting the comparability of other income and expense and the income tax provision include:

- Interest expense increased during the nine months ended September 30, 2010 primarily as a result of higher average outstanding debt balances under our revolving credit facility required for capital expenditures at Calder Casino, financing the repayment of a related party note payable and financing of the acquisition of Youbet.
- Interest income decreased during the nine months ended September 30, 2010 as a result of lower average cash balances due to borrowings made to finance the construction of Calder Casino and the acquisition of Youbet.
- Miscellaneous income increased primarily due to a settlement with ODS. As part of the settlement, a simulcast services agreement was terminated, and the Company received a one-time payment of \$1.3 million.
- Equity in loss of unconsolidated investments decreased primarily as a result of \$0.3 million of equity losses related to our investment in HRTV during the nine months ended September 30, 2010 compared to \$0.5 million of equity losses experienced during the nine months ended September 30, 2009. The improved performance of HRTV is primarily due to increased distribution to ADW businesses and lower distribution costs.
- The effective tax rate decreased during the nine months ended September 30, 2010 compared to the same period of the prior year as a result of an income tax benefit recognized of \$1.6 million reflecting a reduction of interest expense previously estimated to be incurred as a result of the Proposed Audit Adjustment. Additionally, we

## Table of Contents

recognized income tax benefits of \$1.0 million related to the adjustment of permanent differences to reflect positions taken on federal income tax returns. We also recognized \$2.3 million of income tax expense during the nine months ended September 30, 2009 related to the Proposed Audit Adjustment of prior year income tax returns by the IRS.

### Net Revenues By Segment

The following table presents net revenues, including intercompany revenues, by our reported segments (in thousands):

|                         | Nine Months Ended<br>September 30, |                  | Change           |      |
|-------------------------|------------------------------------|------------------|------------------|------|
|                         | 2010                               | 2009             | \$               | %    |
| Churchill Downs         | \$ 99,851                          | \$ 98,156        | \$ 1,695         | 2%   |
| Arlington Park          | 64,075                             | 76,974           | (12,899)         | -17% |
| Calder                  | 43,780                             | 45,038           | (1,258)          | -3%  |
| Fair Grounds            | 32,953                             | 35,853           | (2,900)          | -8%  |
| Total Racing Operations | \$240,659                          | \$256,021        | \$(15,362)       | -6%  |
| Online Business         | 86,622                             | 55,278           | 31,344           | 57%  |
| Gaming                  | 82,824                             | 47,368           | 35,456           | 75%  |
| Other Investments       | 10,203                             | 2,606            | 7,597            | F    |
| Corporate Revenues      | 67                                 | 540              | (473)            | -88% |
| Eliminations            | (9,069)                            | (7,143)          | (1,926)          | -27% |
| Net Revenues            | <u>\$411,306</u>                   | <u>\$354,670</u> | <u>\$ 56,636</u> | 16%  |

Significant items affecting comparability of our revenues by segment include:

- Gaming segment revenues increased primarily as a result of the operation of Calder Casino, which operates over 1,200 slot machines and opened during January 2010. During the nine months ended September 30, 2010, Calder Casino generated total net revenues of \$34.9 million. The Fair Grounds slot facility recognized total net revenues of \$27.7 million during the nine months ended September 30, 2010, which was \$0.5 million higher than total net revenues recognized during the same period of the prior year.

During the nine months ended September 30, 2010, gross gaming revenues of the Fair Grounds slot facility, which is calculated as gross gaming revenues before taxes and promotional deductions but after customer payouts, were \$34.0 million, which was comparable to the same period of the prior year. Gross win per unit at Fair Grounds was \$207 per machine per day during the nine months ended September 30, 2010 compared to \$243 per machine per day during the same period of 2009. At Calder Casino, gross gaming revenues were \$52.6 million, and gross win per unit was \$169 per machine per day during the nine months ended September 30, 2010.

- Online Business revenues increased primarily due to the contribution by Yobet of \$26.2 million of revenues during its four months of operation during the nine months ended September 30, 2010. In addition, revenues increased at TwinSpires and FAW by \$5.2 million, which experienced expansion in average daily wagering during the nine months ended September 30, 2010 compared to the same period of the prior year. This improvement was due, in part, to additional racing content acquired during the nine months ended September 30, 2010, including that from six additional racetracks for which ODS, a major competitor of TwinSpires, previously had exclusive rights. Additionally, we experienced higher wagering on Monmouth Park that we believe was driven by New Jersey gaming-subsidized purses, which contributed to fuller fields.
- Other Investments' revenues increased \$7.6 million primarily due to the addition of United Tote revenues of \$7.8 million during its four months of operation during the nine months ended September 30, 2010.
- Racing Operations revenues decreased primarily due to a decline in pari-mutuel revenues at Arlington Park and Fair Grounds. Arlington Park revenues, particularly those related to export wagering, decreased due to seven fewer race days conducted during the nine months ended September 30, 2010 compared to the same period of the prior year. In addition, we believe competitive pressures, including those resulting from New Jersey gaming-subsidized purses, contributed to fuller fields at Monmouth Park and less wagering on Arlington Park and Calder racing content. Additionally, Arlington Park, during the nine months ended September 30, 2009, recognized \$4.3 million of source

## Table of Contents

market fee revenues related to amounts received from ODS. Fair Grounds revenues declined due to conducting six fewer race days during the nine months ended September 30, 2010 compared to the same period of 2009 and the continued economic weakness in the U.S. economy. Partially offsetting these declines was an increase in revenues at Churchill Downs due to a strong performance from Kentucky Derby week, which more than offset a one-time reduction in pari-mutuel taxes of \$1.7 million during the nine months ended September 30, 2009.

### Segment EBITDA

The following table presents EBITDA by our reported segments (in thousands):

|                   | Nine Months Ended<br>September 30, |                 | Change          |     |
|-------------------|------------------------------------|-----------------|-----------------|-----|
|                   | 2010                               | 2009            | \$              | %   |
| Racing Operations | \$37,819                           | \$41,174        | \$(3,355)       | -8% |
| Online Business   | 14,467                             | 11,767          | 2,700           | 23% |
| Gaming            | 19,537                             | 15,401          | 4,136           | 27% |
| Other Investments | 2,918                              | 1,651           | 1,267           | 77% |
| Corporate         | (2,327)                            | (2,606)         | 279             | 11% |
| Total EBITDA      | <u>\$72,414</u>                    | <u>\$67,387</u> | <u>\$ 5,027</u> | 7%  |

Refer to Note 10 of the Condensed Consolidated Financial Statements included in this Quarterly Report on Form 10-Q for further information about our reported segments, including a reconciliation of EBITDA to earnings from continuing operations.

Significant items affecting comparability of our EBITDA by segment include:

- Gaming EBITDA increased \$4.1 million, reflecting positive EBITDA of \$1.8 million from Calder Casino during the nine months ended September 30, 2010 compared to an EBITDA loss of \$1.2 million generated by preopening expenses incurred during the nine months ended September 30, 2009. Calder Casino's current year EBITDA included allocated corporate overhead of \$1.3 million.
- Online Business EBITDA increased \$2.7 million, which is primarily attributable to the generation of \$2.1 million by Youbet during its four months of operations during the nine months ended September 30, 2010.
- Other Investments EBITDA increased \$1.3 million primarily due to \$1.6 million of EBITDA generated by United Tote during its four months of operations during the nine months ended September 30, 2010.
- Corporate EBITDA increased \$0.3 million and partially reflected a settlement with ODS. As part of the settlement, an underlying simulcast service agreement was terminated, and the Company received a one-time payment of \$1.3 million during the nine months ended September 30, 2010. In addition, legal fees decreased \$1.1 million during the nine months ended September 30, 2010 as we incurred costs related to the bankruptcy filing of MEC and the Illinois riverboat subsidy during the nine months ended September 30, 2009. Finally, there was a decrease of \$1.2 million of compensation expense related to our equity compensation and long-term incentive plans during the nine months ended September 30, 2010 compared to the same period of the prior year. Partially offsetting these increases were additional expenses of \$3.1 million related to the Youbet acquisition.
- Racing Operations EBITDA declined \$3.4 million, which was partially driven by the receipt of \$2.1 million in source market fee revenues, net of purse expense, at Arlington Park during the nine months ended September 30, 2009. In addition, during the nine months ended September 30, 2009, we recognized \$2.5 million in insurance recoveries at Calder and \$2.4 million of real estate tax refunds at Arlington Park. Finally, we experienced a decline in Racing Operations of \$2.9 million related to the deterioration of pari-mutuel business that we believe is caused by 19 fewer race days and a shift in wagering to Monmouth Park. Partially offsetting these declines was a decrease in purse expense of \$1.5 million related to a purse supplement made to the KHBPA during the nine months ended September 30, 2009, a lower allocation of corporate overhead of \$2.2 million and higher EBITDA of \$3.4 million at Churchill Downs from a strong Derby week performance during the nine months ended September 30, 2010.

## Table of Contents

### Discontinued Operations

The following table presents losses from discontinued operations, which includes the result of operations of CDE, Hollywood Park and Ellis Park for the nine months ended September 30, 2010 and 2009 (in thousands):

|  | Nine Months Ended<br>September 30, |                 | Change            |    |
|--|------------------------------------|-----------------|-------------------|----|
|  | 2010                               | 2009            | \$                | %  |
| Net revenues   | \$ 6,303                           | \$ —            | \$ 6,303          | NM |
| Operating expenses   | 12,793                             | —               | 12,793            | NM |
| Selling, general and administrative expenses                                     | 2,060                              | —               | 2,060             | NM |
| Operating loss   | (8,550)                            | —               | (8,550)           | NM |
| Other income (expense):  |                                    |                 |                   |    |
| Miscellaneous, net   | 69                                 | 362             | (293)             | U  |
|  | 69                                 | 362             | (293)             | U  |
| (Loss) earnings from continuing operations before income tax benefit (provision) | (8,481)                            | 362             | (8,843)           | U  |
| Income tax benefit (provision)   | 2,904                              | (1,225)         | 4,129             | F  |
| Net loss   | <u>\$ (5,577)</u>                  | <u>\$ (863)</u> | <u>\$ (4,714)</u> | U  |

### Consolidated Balance Sheet

The following table is a summary of our overall financial position as of September 30, 2010 and December 31, 2009 (in thousands):

|                            | September 30, | December 31, | Change    |     |
|----------------------------|---------------|--------------|-----------|-----|
|                            | 2010          | 2009         | \$        | %   |
| Total assets               | \$ 849,931    | \$ 725,402   | \$124,529 | 17% |
| Total liabilities          | \$ 335,372    | \$ 318,380   | \$ 16,992 | 5%  |
| Total shareholders' equity | \$ 514,559    | \$ 407,022   | \$107,537 | 26% |

Significant items affecting comparability of our consolidated balance sheet include:

- Significant changes within total assets include increases in goodwill of \$68.0 million and other intangible assets of \$22.5 million, which are primarily driven by assets acquired in connection with our acquisition of Youbet.

Additionally, we acquired other assets totaling \$32.3 million in connection with the Youbet acquisition. Other significant changes within total assets include an increase in restricted cash of \$20.4 million. The increase in restricted cash reflects the receipt of \$14.6 million related to the Illinois riverboat subsidy.

Partially offsetting these increases was a decrease in accounts receivable of \$13.7 million, which includes collections of Kentucky Derby-related receivables.

- We assumed \$16.0 million of other liabilities in connection with the Youbet acquisition. Other significant changes within total liabilities include increases in long-term debt and the deferred riverboat subsidy of \$38.4 million and \$14.6 million, respectively. Long-term debt increased due to borrowings of \$45.3 million for the Youbet acquisition and \$24.0 million used to repay the Arlington Park land note, partially offset by \$31.0 million in repayments funded by cash flows provided by operations. The deferred riverboat subsidy increased, reflecting the receipt of additional monies related to the Illinois riverboat subsidy.

## Table of Contents

Partially offsetting these increases was a decrease in deferred revenue of \$14.5 million due to the recognition of advance billings related to the 2010 Kentucky Derby and the 2010 spring meet at Churchill Downs.

### Liquidity and Capital Resources

The following table is a summary of our liquidity and cash flows (in thousands):

|                                    | Nine Months Ended<br>September 30, |            | Change     |      |
|------------------------------------|------------------------------------|------------|------------|------|
|                                    | 2010                               | 2009       | \$         | %    |
| <b>Cash Provided by (used) in:</b> |                                    |            |            |      |
| Operating activities               | \$ 55,341                          | \$ 62,869  | \$ (7,528) | -12% |
| Investing activities               | \$(92,072)                         | \$(40,634) | \$(51,438) | U    |
| Financing activities               | \$ 37,621                          | \$(18,341) | \$ 55,962  | F    |

- The decrease in cash provided by operating activities is primarily due to operating losses incurred by CDE during the nine months ended September 30, 2010. We anticipate that cash flows from operations, including those associated with the acquisition of Youbet, over the next twelve months will be adequate to fund our business operations and capital expenditures.
- The increase in cash used in investing activities during the nine months ended September 30, 2010 is primarily attributable to capital expenditures related to the construction of Calder Casino and the purchase of Arlington Park land in addition to the acquisition of Youbet. As of September 30, 2010, we have spent a total of \$79.3 million to build Calder Casino.
- Cash flows from financing activities increased as we borrowed in excess of our repayments on our revolving loan facilities by \$38.4 million during the nine months ended September 30, 2010, primarily to fund the expansion of our gaming operations and the acquisition of Youbet.

During the nine months ended September 30, 2010, there were several material changes in our commitments to make future payments. During the second quarter of 2010, we borrowed under our revolving credit facility to finance the cash portion of the consideration paid in connection with the acquisition of Youbet, which was \$45.3 million. In addition, we borrowed \$24.0 million under our revolving credit facility to pay the note payable to Duchossois Industries, a related party, which financed the purchase of land at Arlington Park. During the third quarter of 2010, we funded \$2.8 million of annual licensing fees for Calder Casino. We anticipate borrowing \$138.0 million during the fourth quarter of 2010 to finance the acquisition of Harlow's Casino Resort and Hotel. As of September 30, 2010, we were in compliance with the debt covenants of our revolving credit facility.

### Credit Facilities and Indebtedness

#### *Second Amended and Restated Credit Agreement*

On November 1, 2010, we entered into Amendment No. 1 to the Second Amended and Restated Credit Agreement (the "Amendment"), which amends certain provisions of the credit agreement and provides for the exercise of the accordion feature whereby the maximum aggregate commitment will be increased from \$275 million to \$375 million. Additionally, the Amendment reduces the pricing schedule for outstanding borrowings by 37.5 basis points and commitment fees by 5 basis points across all leverage pricing levels. The guarantors under the credit agreement continue to be a majority of the Company's wholly-owned subsidiaries. We also incurred loan origination costs of approximately \$0.4 million in connection with the Amendment, which will be capitalized and will be amortized as interest expense over the remaining term of the credit agreement. The facility terminates on December 22, 2013.

Generally, borrowings made pursuant to the Amendment will bear interest at a LIBOR-based rate per annum plus an applicable percentage ranging from 1.625% to 3.125% depending on certain of the Company's financial ratios. In addition, under the Amendment, we agreed to pay a commitment fee at rates that range from 0.25% to 0.45% of the available aggregate commitment, depending on the Company's leverage ratio.

The Credit Facility contains customary affirmative and negative covenants for credit facilities of this type, including limitations on the Company and its subsidiaries with respect to indebtedness, restricted payments, liens, investments, mergers and acquisitions, disposition of assets, sale-leaseback transactions, and transactions with affiliates. The covenants permit the Company to use proceeds of the credit extended under the agreement for general corporate purposes and acquisition needs. The Credit Facility also contains financial covenants that require the Company (i) to maintain an interest coverage ratio (i.e.,

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## Table of Contents

consolidated adjusted EBITDA to consolidated interest expense) that is greater than 3.5 to 1.0; (ii) not to permit the leverage ratio (i.e., consolidated funded indebtedness to consolidated adjusted EBITDA) to be greater than 3.25 to 1.0; and (iii) to maintain consolidated net worth (with certain exceptions) of not less than the sum of (x) \$350,000,000, (y) 50% of consolidated net income earned in each fiscal year beginning with the Company's fiscal year ending December 31, 2009 and (z) 100% of the net proceeds of any future debt and equity offerings. Substantially all of the Company's assets continue to be pledged as collateral under the Credit Facility.

### ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

At September 30, 2010, we had \$110.3 million outstanding under our revolving credit facility, which bears interest at LIBOR based variable rates. We are exposed to market risk on variable rate debt due to potential adverse changes in these rates. Assuming the outstanding balance of the debt facilities remain constant, a one-percentage point increase in the LIBOR rate would reduce annual pre-tax earnings, recorded fair value and cash flows by \$1.1 million.

### ITEM 4. CONTROLS AND PROCEDURES

#### (a) Evaluation of Disclosure Controls and Procedures

As of the end of the period covered by this report, the Company carried out an evaluation, under the supervision and with the participation of the Company's Disclosure Committee and management, including the Chief Executive Officer and the Chief Financial Officer, of the effectiveness of the design and operation of our disclosure controls and procedures pursuant to Exchange Act Rule 13a-15(b). Based upon this evaluation, the Chief Executive Officer and the Chief Financial Officer concluded that our disclosure controls and procedures were effective as of September 30, 2010.

#### (b) Changes in Internal Control Over Financial Reporting

Management of the Company has evaluated, with the participation of the Company's Chief Executive Officer and Chief Financial Officer, changes in the Company's internal control over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act) during the quarter ended September 30, 2010. There have not been any changes in the Company's internal control over financial reporting (as defined in Rule 13a-15(f) of the Exchange Act) that occurred during the quarter ended September 30, 2010 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

## PART II. OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS

#### YOUBET ACQUISITION

On November 17, 2009, a putative class action lawsuit, *Wayne Witkowski v. Youbet.com, Inc., et al.*, was filed in the Superior Court of Los Angeles, California against Youbet, various of its directors, the Company and the Company's wholly-owned subsidiaries, Tomahawk Merger Corp. ("Merger Sub") and Tomahawk Merger LLC ("Merger LLC"). Subsequently, five additional lawsuits were also filed in the Los Angeles Superior Court, two of which name Youbet and its directors as defendants and three of which also name the Company as a defendant. All six lawsuits (collectively, the "Los Angeles Litigation"), are putative class actions brought on behalf of Youbet's stockholders. Plaintiffs in the Los Angeles litigation moved to consolidate the Los Angeles Litigation, to file a single consolidated complaint and to appoint lead counsel. That motion was granted on January 22, 2010.

The complaints in the Los Angeles Litigation all allege that Youbet's directors breached their fiduciary duties, including alleged duties of loyalty, due care and candor, in connection with the sale of Youbet. In that regard, the various complaints include, among other things, allegations that the sale of Youbet is the result of an inadequate sales process which has not been designed to maximize stockholder value; that the consideration to be received by Youbet stockholders is unfair and inadequate; that the merger agreement includes inappropriate "no solicitation," "matching rights," no standstill waiver, and termination fee provisions; that the combined effect of these provisions, together with Youbet's waiver of the Youbet stockholder rights agreement with respect to the Company and the entry of voting agreements by defendants and certain others pursuant to which they have agreed to vote in favor of the sale of Youbet, was to "lock up" the sale of Youbet, foreclose potential alternative bidders and illegally restrain Youbet's ability to solicit or engage in negotiations with a third party; that various defendants acted for their own benefit in approving the sale of Youbet, including for the purpose of obtaining positions or pursuing opportunities at the Company; and that material information was not provided in connection with the sale of Youbet and was not provided at the time that Youbet submitted the Youbet stockholder rights agreement to a stockholder vote. Those lawsuits which name the Company or its affiliates as defendants also allege that the Company has

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## Table of Contents

aided and abetted the alleged breaches of fiduciary duty by Youbet's directors. Youbet is also alleged to have aided and abetted the alleged breaches of fiduciary duty by its directors. Among the relief sought by the complaints is an enjoining of the sale of Youbet, together with payment of attorneys' fees and costs.

On December 23, 2009, a putative class action lawsuit, *Raymond Balch v. Youbet.com, Inc., et al.*, was filed in the Delaware Court of Chancery against Youbet, various of its directors, the Company, Merger Sub and Merger LLC alleging claims similar to the Los Angeles Litigation. On January 8, 2010, Mr. Balch amended his complaint to add counts asserting that Youbet's directors breached their fiduciary duties to Youbet stockholders by allegedly failing to disclose material information regarding the sale of Youbet in a preliminary registration statement filed with the Securities and Exchange Commission on December 24, 2009 and that Youbet and the Company aided and abetted such alleged breaches.

On March 2, 2010, Youbet, Youbet's directors, the Company, Merger Sub, and Merger LLC entered into a memorandum of understanding with the plaintiffs in the Los Angeles Litigation and the plaintiffs in the *Balch* litigation reflecting an agreement in principle to settle the cases based on, among other things, defendants' agreement to include in an amended registration statement certain additional disclosures relating to the sale of Youbet. The memorandum of understanding provides that the settlement is subject to customary conditions including the completion of appropriate settlement documentation and completion of confirmatory discovery. Pursuant to the memorandum of understanding, an amended registration statement was filed containing the additional agreed disclosures.

On or about July 14, 2010, the parties to the Los Angeles Litigation and the *Balch* litigation entered into a settlement agreement consistent with the terms of the memorandum of understanding. The settlement agreement provides, among other things, for a certification of a class for settlement purposes, dismissal with prejudice of the Los Angeles Litigation and the *Balch* litigation, releases by class members and payment of attorneys' fees and expenses approved by the court. The settlement agreement is subject to court approval. In both the memorandum of understanding and the settlement agreement, Youbet, Youbet's directors, the Company, Merger Sub, and Merger LLC each deny that they have committed or aided and abetted in the commission of any violation of law or engaged in any of the wrongful acts alleged in the complaints, and expressly maintain that they diligently and scrupulously complied with any and all of their legal duties. Although Youbet, Youbet's directors, the Company, Merger Sub, and Merger LLC believe the lawsuits are without merit, they entered into the memorandum of understanding and settlement to eliminate the burden and expense of further litigation. On July 14, 2010, plaintiffs in the Los Angeles Litigation filed the settlement agreement with the Superior Court of California, County of Los Angeles, together with a request for preliminary approval of the settlement and of a proposed class notice and for the scheduling of a hearing date for final approval of the settlement. On August 19, 2010, the court presiding over the Los Angeles litigation granted preliminary approval to the proposed settlement and scheduled a final approval hearing date of December 20, 2010.

If the settlement is consummated, the Los Angeles Litigation and the *Balch* litigation will each be dismissed with prejudice and the defendants and other released persons will receive from or on behalf of all of Youbet's non-affiliated public stockholders who held Youbet common stock at any time from November 10, 2009 through the date of the consummation of the merger a release of, among other things, all claims relating to the sale of Youbet, the merger agreement and the transactions contemplated therein, disclosures made relating to the sale of Youbet, and any compensation or other payments made to the defendants in connection with the sale of Youbet. The release does not apply to the right of any Youbet stockholder or former Youbet stockholder who has taken the steps required by Delaware law to seek appraisal of his or her Youbet shares from pursuing an appraisal in accordance with Delaware law. Plaintiffs will also receive a release from the defendants with respect to all claims arising out of, relating to, or in connection with the institution, prosecution, assertion or resolution of the lawsuits. We will not incur any significant loss or expense as a result of this settlement.

## CLOVERLEAF

On July 7, 2009, Cloverleaf Enterprises, Inc. (d/b/a Rosecroft Raceway) ("Cloverleaf") filed a lawsuit styled *Cloverleaf Enterprises, Inc. vs. Maryland Thoroughbred Horsemen's Association, Inc., et al.*, (Case No. 09-00459 PM) in the United States Bankruptcy Court, District of Maryland, Greenbelt Division. This adversary proceeding named the Company, Arlington Park and Calder (the "Named CDI Entities") as defendants, along with TrackNet, certain Maryland thoroughbred entities and other racetracks outside of Maryland. Cloverleaf alleged that the defendants breached simulcast agreements to send audio-visual signals of their live thoroughbred horse races and that certain defendants, including TrackNet, tortiously interfered with simulcast agreements in which Cloverleaf entered. On November 16, 2009, Cloverleaf filed an amended complaint (the "Amended Complaint") which asserted antitrust claims against certain of the defendants, but not the Company or TrackNet. On December 23, 2009, Cloverleaf dismissed the tortious interference claim against TrackNet, which left only breach of contract claims against TrackNet and the Company. The Company and TrackNet answered the Amended Complaint on January 12, 2010, denying the breach of contract claims.

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## Table of Contents

The Maryland racing defendants subsequently moved to dismiss the Amended Complaint and to withdraw the reference to the bankruptcy court. On February 23, 2010, after the motion to withdraw the reference went unopposed, the adversary proceeding was transferred to the United States District Court, District of Maryland, and assigned Case No. 10-0407 (“RDB”). The Company is vigorously defending against this lawsuit. On May 14, 2010, the Company and TrackNet jointly moved for summary judgment on Cloverleaf’s breach of contract claims against them. Briefing on the motion for summary judgment is complete, and a motions hearing was held on July 29, 2010. The motions hearing also included the Maryland racing defendants’ motion to dismiss. On August 25, 2010, the court granted our motion for summary judgment. On September 20, 2010, Cloverleaf filed a motion to reconsider. We have filed our response opposing this motion. The court has not yet ruled on Cloverleaf’s motion to reconsider.

### **FLORIDA QUARTER HORSE TRACK ASSOCIATION, INC.**

On July 21, 2010, the Florida Quarter Horse Track Association, Inc. (the “FQHTA”) filed a lawsuit styled *Florida Horse Track Association, Inc. vs. State of Florida, Department of Business and Professional Regulation, Division of Pari-Mutuel Wagering, Calder Race Course, Inc. and Tropical Park, Inc.*, (Case No. 2010 CA 2519) in the Circuit Court of the Second Judicial Circuit in and for Leon County, Florida. The FQHTA alleges that: 1) the Florida statute that authorizes the issuance of the original thoroughbred racing permit to Calder in 1969 was an unconstitutional special law under the Florida constitution, and 2) the arrangement between Tropical Park and Calder under which Tropical Park conducts its race meets at Calder is not authorized by the Florida statutes. The case is pending in Leon County, Florida.

### **OTHER MATTERS**

There are no other pending material legal proceedings, other than ordinary routine litigation incidental to our business, to which we are a party or any of our property is the subject, and no such proceedings are known to be contemplated by governmental authorities.

### **ITEM 1A. RISK FACTORS**

Information regarding risk factors appears in Part I – Item 1A, “Risk Factors” of the Company’s Annual Report on Form 10-K for the year ended December 31, 2009. There have been no material changes from the risk factors previously disclosed in the Company’s Annual Report on Form 10-K.

In addition to risks and uncertainties in the ordinary course of business that are common to all businesses, important factors that are specific to our industry and company could materially impact our future performance and results. The factors described in Part I – Item 1A, “Risk Factors” of our Annual Report on Form 10-K are the most significant risks that could materially impact our business, financial condition and results of operations. Additional risks and uncertainties that are not presently known to us, that we currently deem immaterial or that are similar to those faced by other companies in our industry or business in general may also impair our business and operations. Should any risks or uncertainties develop into actual events, these developments could have a material, adverse impact on our business, financial condition and results of operations.

## Table of Contents

### ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS

The following table provides information with respect to shares of common stock repurchased by the Company during the quarter ended September 30, 2010:

|          |                 | <u>Total Number of<br/>Shares Purchased</u> | <u>Average Price<br/>Paid Per Share</u> | <u>Total Number of<br/>Shares Purchased<br/>as Part of Publicly<br/>Announced Plans<br/>or Programs</u> | <u>Approximate Dollar<br/>Value of Shares<br/>That May Yet Be<br/>Purchased under<br/>the Plans or<br/>Programs</u> |
|----------|-----------------|---|---|---|---|
| Period 1 | 7/1/10- 7/31/10 | —   | —                                       | —   | —   |
| Period 2 | 8/1/10- 8/31/10 | —   | —                                       | —   | —   |
| Period 3 | 9/1/10- 9/30/10 | 11,665 <sup>(1)</sup>                       | \$ 34.98                                | —   | —   |
|          |                 | <u>11,665</u>                               | <u>\$ 34.98</u>                         | <u>—</u>  | <u>—</u>  |

(1) Shares of common stock were repurchased from grantee of restricted stock in payment of income taxes on the related compensation.

### ITEM 3. DEFAULTS UPON SENIOR SECURITIES

Not applicable.

### ITEM 4. REMOVED AND RESERVED

### ITEM 5. OTHER INFORMATION

Not applicable.

### ITEM 6. EXHIBITS

See Exhibit Index.

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**Table of Contents**

**SIGNATURES**

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

November 3, 2010

**CHURCHILL DOWNS INCORPORATED**

/s/ Robert L. Evans

Robert L. Evans  
President and Chief Executive Officer  
(Principal Executive Officer)

November 3, 2010

/s/ William E. Mudd

William E. Mudd  
Executive Vice President and Chief  
Financial Officer  
(Principal Financial and Accounting Officer)

**EXHIBIT INDEX**

| <b><u>Number</u></b> | <b><u>Description</u></b>  | <b><u>By Reference To</u></b>   |
|----------------------|--|---|
| 10(a)                | Amended and Restated Employment Agreement dated as of September 27, 2010, by and between Churchill Downs Incorporated and Robert L. Evans. *                                   | Quarterly Report on Form 10-Q for the fiscal quarter ended September 30, 2010 |
| 31(i)(a)             | Certification of Chief Executive Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002   | Quarterly Report on Form 10-Q for the fiscal quarter ended September 30, 2010 |
| 31(i)(b)             | Certification of Chief Financial Officer Pursuant to Section 302 of the Sarbanes-Oxley Act of 2002   | Quarterly Report on Form 10-Q for the fiscal quarter ended September 30, 2010 |
| 32                   | Certification of CEO and CFO Pursuant to 18 U.S.C. Section 1350, As Adopted Pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (furnished pursuant to Rule 13a – 14(b)) | Quarterly Report on Form 10-Q for the fiscal quarter ended September 30, 2010 |

\* Portions of this agreement have been redacted pursuant to a confidential treatment request filed with the Securities Exchange Commission. Such redacted portions have been marked with an asterisk.

## AMENDED AND RESTATED EMPLOYMENT AGREEMENT

THIS AMENDED AND RESTATED EMPLOYMENT AGREEMENT (this “Agreement”) is dated as of September 27, 2010 (the “Effective Date”), by and between Churchill Downs Incorporated, a Kentucky corporation (the “Company”), and Robert L. Evans (“Executive”).

WHEREAS, the Company and Executive are parties to that certain employment agreement, dated as of August 14, 2006, as amended by the First Amendment to Employment Agreement dated November 25, 2008 (collectively, the “Prior Employment Agreement”);

WHEREAS, the Company desires to continue Executive’s employment and to amend and restate the Prior Employment Agreement to embody the terms of such continued employment, and considers it to be in its best interests and in the best interests of its stockholders to employ Executive during the Employment Term (as defined in Section 1 below);

WHEREAS, Executive desires to accept such continued employment with the Company and to amend and restate the Prior Employment Agreement; and

WHEREAS, Executive is willing to accept continued employment on the terms hereinafter set forth in this Agreement.

NOW, THEREFORE, in consideration of the premises and mutual covenants herein and for other good and valuable consideration, the parties hereby agree as follows:

1. Term of Employment . Unless terminated earlier in accordance with the provisions of Section 7, Executive’s employment under this Agreement shall be effective for a term commencing on the Effective Date and ending on August 14, 2016 (the “Employment Term”). Thereafter, the Employment Term shall be automatically extended for subsequent one (1)-year periods unless written notice to the contrary is given by either the Company or Executive at least ninety (90) days prior to the expiration of the Employment Term or the expiration of any subsequent one (1)-year extension thereof.

2. Position and Duties .

(a) As of the Effective Date, Executive shall continue to serve as the Chief Executive Officer and President of the Company. In such position, Executive shall report directly to the Board (as defined in Section 10(c)) and have such authority, responsibilities, and duties customarily exercised by a person holding such position. During the Employment Term, the Company shall cause Executive to be nominated for election as a member of the Board as needed to maintain Executive’s position on the Board.

(b) During the Employment Term, Executive will devote substantially all of his business time and best efforts to the performance of his duties. Executive may:

(i) in addition to being a director of the Company and with the prior written approval of the Chairman of the Board, serve as a director or trustee of: (x) up to three (3) corporate or charitable entities; and (y) trade or other associations related to the Company’s industry; and

(ii) manage his personal investments;

to the extent that such activities do not materially inhibit or materially interfere with the performance of Executive's duties under this Agreement.

3. Base Salary. During the Employment Term, the Company shall pay Executive a base salary (the "Base Salary") at the annual rate of \$550,000.00, payable in regular installments in accordance with the Company's usual payroll practices. The Base Salary includes fees otherwise payable for his services for the Board. The Board shall review and may consider for increase (but not decrease) at any time Executive's Base Salary in its sole discretion based on Executive's performance.

4. Incentive Compensation. Executive shall be eligible to participate in any annual or long-term, cash or equity based, incentive plan or other arrangements of the Company, as they exist from time-to-time. Executive shall be eligible to participate in an annual performance bonus plan, with a target bonus for each performance period of 100% of Base Salary.

5. Equity Grants. Executive shall retain all outstanding equity grants provided in the Prior Employment Agreement, whether or not vested as of the Effective Date, in accordance with the terms of the Prior Employment Agreement and applicable plan documents and award agreements, and shall also receive the following additional equity grants:

(a) Restricted Shares.

(i) As of the Effective Date, the Company shall grant Executive 45,000 Restricted Shares of Common Stock which shall vest as follows upon the Fair Market Value (as defined in Section 10(m)) of a share of the Common Stock (as defined in Section 10(g)) reaching the following prices for twenty (20) consecutive trading days beginning on and after August 14, 2011; provided, however, that such twenty (20)-trading day period occurs prior to a Termination of Employment (as defined in Section 10(u)), but subject to Section 7(b) below:

| <u>20 Day Fair Market Value<br/>at or Above</u> | <u>Shares Vesting</u> |
|---|-----------------------|
| \$**.**   | 15,000                |
| \$**.**   | 15,000                |
| \$**.**   | 15,000                |

\* Confidential information omitted and filed separately with the Securities and Exchange Commission under a Confidential Treatment Request.

(ii) As of the Effective Date, the Company shall grant Executive 81,250 Restricted Shares of Common Stock which shall vest for the applicable number of Restricted Shares per the corresponding vesting date as listed on the schedule below; provided, however, that such vesting date occurs prior to a Termination of Employment, but subject to Section 7(b) below:

| <u>Vesting Date</u> | <u>Shares Vesting</u> |
|---------------------|-----------------------|
| September 30, 2011  | 2,032                 |
| December 31, 2011   | 4,062                 |
| March 31, 2012      | 4,063                 |
| June 30, 2012       | 4,062                 |
| September 30, 2012  | 4,063                 |
| December 31, 2012   | 4,062                 |
| March 31, 2013      | 4,063                 |
| June 30, 2013       | 4,062                 |
| September 30, 2013  | 4,063                 |
| December 31, 2013   | 4,062                 |
| March 31, 2014      | 4,063                 |
| June 30, 2014       | 4,062                 |
| September 30, 2014  | 4,063                 |
| December 31, 2014   | 4,062                 |
| March 31, 2015      | 4,063                 |
| June 30, 2015       | 4,062                 |
| September 30, 2015  | 4,063                 |
| December 31, 2015   | 4,062                 |
| March 31, 2016      | 4,063                 |
| June 30, 2016       | 4,062                 |
| August 14, 2016     | 2,031                 |

(b) Stock Options. As of the Effective Date, the Company shall grant Executive Options (as defined in Section 10(p)), with a term until no later than November 14, 2016, to purchase 180,000 shares of Common Stock with a per share exercise price equal to the Fair Market Value of a share of Common Stock as of the date of grant. Such Options shall vest as follows:

| <u>Vesting Date</u> | <u>Number of Options to Vest</u> |
|---------------------|----------------------------------|
| September 30, 2010  | 7,500                            |
| December 31, 2010   | 15,000                           |
| March 31, 2011      | 15,000                           |
| June 30, 2011       | 15,000                           |
| September 30, 2011  | 15,000                           |
| December 31, 2011   | 15,000                           |
| March 31, 2012      | 15,000                           |
| June 30, 2012       | 15,000                           |
| September 30, 2012  | 15,000                           |
| December 31, 2012   | 15,000                           |
| March 31, 2013      | 15,000                           |
| June 30, 2013       | 15,000                           |
| August 14, 2013     | 7,500                            |

(c) Change in Control. In the event of a Change in Control during the Employment Term, Executive shall receive accelerated vesting of: (i) fifty percent (50%) of the then-unvested Restricted Stock Units granted pursuant to the Prior Employment Agreement, (ii) fifty percent (50%) of the then-unvested Restricted Shares granted pursuant to Subsections 5(a)(i) and (ii) above and the Prior Employment Agreement, and (iii) fifty percent (50%) of the then-unvested Options granted pursuant to Section 5(b) above. The Restricted Stock Units, Restricted Shares and Stock Options that are subject to accelerated vesting pursuant to this Section 5(c) shall be taken pro-rata from each then-unvested tranche of the applicable award, and the remaining portion of each tranche shall vest according to the original terms of the applicable award agreement, subject to potential accelerated vesting pursuant to Section 7(c) below.

#### 6. Other Benefits.

(a) Retirement Benefits. During the Employment Term, Executive shall be provided with the opportunity to participate in the Company's qualified 401(k) profit sharing plan and non-qualified deferred compensation plan, as may exist from time-to-time, in each case, in accordance with the terms of such plans.

(b) Welfare Benefits. During the Employment Term, Executive shall be provided with the opportunity to participate in the Company's medical plan and other employee welfare benefit plans on a comparable basis as such benefits are generally provided by the Company from time-to-time to the Company's other senior executives, in each case, in accordance with the terms of such plans.

(c) Perquisites. During the Employment Term, Executive shall be provided with the opportunity to receive or participate in perquisites on a comparable basis as such perquisites are generally provided by the Company from time-to-time to the Company's other senior executives, subject to the following:

(i) Transportation benefit – Executive will be entitled to transportation, via car service or other comparable arrangement, in connection with the performance of his duties hereunder (including but not limited to transportation between his primary residence and the Main Office (as defined in Section 10(o)), which will be in lieu of the Company's standard cash automobile subsidy provided to senior executives. To the extent this benefit is taxable income to Executive, he will receive a Tax Gross-Up Payment (as defined in Section 10(t)); and

(ii) Attorney fees – The Company will pay reasonable attorneys' fees and related expenses incurred by Executive in connection with the negotiation and review of this Agreement up to a maximum of \$5,000.

(iii) Indemnification Agreement. The July 18, 2006 Indemnification Agreement between the parties, or any subsequent indemnification agreement between the parties that provides no fewer protections for Executive, shall remain in full force and effect during the Employment Term.

(d) Reimbursement of Business Expenses. During the Employment Term, all reasonable business expenses incurred by Executive in the performance of his duties hereunder shall be reimbursed by the Company upon receipt of documentation of such expenses in a form

reasonably acceptable to the Company, and otherwise in accordance with the Company's expense reimbursement policies. Pursuant to the terms of this Section 6(d), the Company shall pay for the reasonable expenses of Executive's wife when she travels with him on the Company's business. Any reimbursement payment shall be made no later than the end of Executive's taxable year following the taxable year in which the expense is incurred.

7. Termination. Notwithstanding any other provision of this Agreement:

(a) For Cause by the Company or Voluntary Resignation by Executive Without Good Reason. If Executive is terminated by the Company for Cause (as defined in Section 10(d)) or if Executive voluntarily resigns without Good Reason (as defined in Section 10(n)), Executive shall be entitled to receive as soon as reasonably practicable after his date of termination or such earlier time as may be required by applicable statute or regulation: (i) his earned but unpaid Base Salary through the date of termination; (ii) payment in respect of any vacation days accrued but unused through the date of termination, to the extent provided by Company policy; (iii) reimbursement for all business expenses properly incurred in accordance with Company policy prior to the date of termination and not yet reimbursed by the Company; and (iv) subject to Section 7(g), any earned but unpaid annual bonus in respect of any of the Company's fiscal years preceding the fiscal year in which the termination occurs (provided, however, that if Executive's termination is by the Company for Cause and such event(s) and/or action(s) that constitute Cause are materially and demonstrably injurious to the business or reputation of the Company, then no payment will be made pursuant to this clause (iv)) (the aggregate benefits payable pursuant to clauses (i), (ii), (iii) and (iv) hereafter referred to as the "Accrued Obligations"); and except as provided herein he shall have no further rights to any compensation (including any Base Salary or annual bonus, if any) or any other benefits under this Agreement. All equity-based awards shall be treated as set forth under the terms of the Prior Employment Agreement, this Agreement and the applicable plan or agreement. All other accrued and vested benefits, if any, due Executive following Executive's Termination of Employment pursuant to this Section 7(a) shall be determined and provided or paid in accordance with the plans, policies, and practices of the Company; provided such benefits shall be provided or paid no later than the later of (A) sixty (60) days following Executive's date of termination or (B) the date provided under the applicable plan, policy or practice of the Company covering such benefits.

(b) Without Cause by the Company or Voluntary Resignation by Executive for Good Reason. If Executive is terminated by the Company other than for Cause, Disability (as defined in Section 10(i)) or death, or if Executive voluntarily resigns for Good Reason, Executive shall receive: (i) the Accrued Obligations; and (ii) subject to Section 7(g), (A) cash payments equal to the product of 1.5 times the sum of (x) Executive's Base Salary plus (y) Executive's target bonus for the year of the Termination of Employment, payable in equal installments over the 18 months following Termination of Employment, (B) treatment of all equity-based awards per the terms of the Prior Employment Agreement, this Agreement and the applicable plan or agreement; provided, however, that vesting of any equity awards granted pursuant to Section 5 of this Agreement and the Prior Employment Agreement (including Restricted Shares vesting upon achievement of certain stock price targets) shall be calculated through the end of the calendar quarter in which Termination of Employment occurs, and (C) the continuation of medical benefits through the end of the calendar quarter in which Termination of Employment occurs; provided, however, that such benefit shall be reduced or eliminated to the

extent Executive receives similar benefits from a subsequent employer. Except as provided herein, Executive shall have no further rights to any compensation (including any Base Salary) or any other benefits under this Agreement. All other accrued and vested benefits, if any, due Executive following Termination of Employment pursuant to this Section 7(b) shall be determined and provided or paid in accordance with the plans, policies and practices of the Company; provided such benefits shall be provided or paid no later than the later of (A) sixty (60) days following Executive's date of termination or (B) the date provided under the applicable plan, policy or practice of the Company covering such benefits.

(c) Termination following a Change in Control. If, during the 2-year period following a Change in Control (as defined in Section 10 (e)), Executive is terminated by the Company other than for Cause, Disability or death, or if Executive voluntarily resigns for Good Reason, Executive shall receive: (i) the Accrued Obligations; and (ii) subject to Section 7(g), (A) the benefits set forth in Section 7(b)(ii) (with any payments due pursuant to clause (A) of Section 7(b)(ii) payable in a lump sum on the sixtieth (60th) day following such Termination of Employment), (B) full accelerated vesting of (x) any then-unvested Restricted Stock Units granted pursuant to the Prior Employment Agreement, (y) any then-unvested Restricted Shares granted pursuant to Subsections 5(a)(i) and (ii) above and the Prior Employment Agreement, and (z) any then-unvested Stock Options granted pursuant to Section 5(b) above, and (C) a Tax Gross-Up Payment for purposes of Code Section 280G.

(d) Death. Following a Termination of Employment for death, Executive's estate shall be entitled to receive: (i) the Accrued Obligations; and (ii) subject to Section 7(g), (A) a pro-rata bonus, if any, for the year of death, based on the target bonus for which Executive was eligible for such year, and paid when bonuses under such applicable bonus plans are normally paid, (B) (x) with respect to the Restricted Stock award described in Section 5(a)(ii) above (granting 81,250 restricted shares), vesting in any shares that otherwise would have vested over the 18 months following the date of termination pursuant to Executive's continued employment with the Company and (y) treatment of all other equity-based awards per the terms of the Prior Employment Agreement, this Agreement and the applicable plan or agreement, (C) all other benefits and payments per the applicable plan or program, and (D) life insurance benefits paid per such applicable plans. Except as provided herein, Executive's estate shall have no further rights to any compensation (including any Base Salary) or any other benefits under this Agreement. All other accrued and vested benefits, if any, due Executive following a Termination of Employment for death shall be determined in accordance with the plans, policies, and practices of the Company.

(e) Disability. Following a Termination of Employment for Disability, Executive shall be entitled to receive: (i) the Accrued Obligations; and (ii) subject to Section 7(g), (A) a pro-rata bonus, if any, for the year of Termination of Employment, based on the target bonus for which Executive was eligible for such year, and paid when bonuses under the applicable bonus plans are normally paid, (B) (x) with respect to the Restricted Stock award described in Section 5(a)(ii) above (granting 81,250 restricted shares), vesting in any shares that otherwise would have vested over the 18 months following the date of termination pursuant to Executive's continued employment with the Company and (y) treatment of all other equity-based awards per the terms of the Prior Employment Agreement, this Agreement and the applicable plan or agreement, (C) all other benefits and payments per the applicable plan or program, and (D) short-term and long-term disability benefits per the applicable plans. Except as provided

herein, Executive shall have no further rights to any compensation (including any Base Salary) or any other benefits under this Agreement. All other accrued and vested benefits, if any, due Executive following a Termination of Employment for Disability shall be determined in accordance with the plans, policies, and practices of the Company.

(f) No Mitigation or Offset. In no event shall the benefits set forth in this Section 7 be subject to mitigation or offset.

(g) Release. Notwithstanding any other provision of this Agreement to the contrary, Executive acknowledges and agrees that any and all payments to which Executive is entitled under this Section 7, which are described as being subject to this Section 7(g) are conditioned upon and shall not be payable unless (A) Executive, or, if applicable, his or his estate's personal representative, executes a general release and waiver, in such reasonable and customary form as shall be prepared by the Company, of all claims Executive may have against the Company and its directors, officers, subsidiaries and affiliates, except as to (i) matters covered by provisions of this Agreement that expressly survive the termination of this Agreement and (ii) rights to which Executive is entitled by virtue of his participation in the employee benefit plans, policies and arrangements of the Company, within the minimum time period required under applicable state and federal laws, or if no such period, ten business days following the date of Executive's termination, and (B) Executive, or, if applicable, his or his estate's personal representative, has not revoked such release agreement within the time permitted under applicable law. Payments subject to this Section 7(g) shall commence or be made, as applicable, on the sixtieth (60th) day after the Termination of Employment, with any payments scheduled to occur between the Termination of Employment and such sixtieth (60th) day provided on such day.

## 8. Covenants.

(a) Confidentiality. Executive agrees that Executive will not at any time during Executive's employment with the Company or thereafter, except in performance of Executive's obligations to the Company hereunder, disclose, either directly or indirectly, any Confidential Information (as hereinafter defined) that Executive may learn by reason of his association with the Company. The term "Confidential Information" shall mean any past, present, or future confidential or secret plans, programs, documents, agreements, internal management reports, financial information, or other material relating to the business, strategies, services, or activities of the Company, including, without limitation, information with respect to the Company's operations, processes, products, inventions, business practices, finances, principals, vendors, suppliers, customers, potential customers, marketing methods, costs, prices, contractual relationships, including leases, regulatory status, compensation paid to employees, or other terms of employment, and trade secrets, market reports, customer investigations, customer lists, and other similar information that is proprietary information of the Company; provided, however, the term "Confidential Information" shall not include any of the above forms of information which has become public knowledge, unless such Confidential Information became public knowledge due to any act or acts by Executive or his representative(s) in violation of this Agreement. Notwithstanding the foregoing, Executive may disclose such Confidential Information when required to do so by a court of competent jurisdiction, by any governmental agency having supervisory authority over the business of the Company and/or its affiliates, as the case may be, or by any administrative body or legislative body (including a committee thereof) with jurisdiction to order Executive to divulge, disclose or make accessible such information;

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provided, further, that in the event that Executive is ordered by any such court or other government agency, administrative body, or legislative body to disclose any Confidential Information, Executive shall (i) promptly notify the Company of such order, (ii) at the reasonable written request of the Company, diligently contest such order at the sole expense of the Company as expenses occur, and (iii) at the reasonable written request of the Company, seek to obtain, at the sole expense of the Company, such confidential treatment as may be available under applicable laws for any information disclosed under such order.

(b) Non-Compete. During the Employment Term and for two (2) years immediately following a Termination of Employment for any reason, Executive shall not, without the prior written consent of the Company, participate or engage in, directly or indirectly (as an owner, partner, employee, officer, director, independent contractor, consultant, advisor or in any other capacity calling for the rendition of services, advice, or acts of management, operation or control) any business for a Competitor (as defined below). The term “Competitor” shall mean any entity whose principal business involves the operation of a pari-mutuel or casino gaming or advance deposit wagering business .

(c) Non-Solicit. During the Employment Term and for two (2) years immediately following a Termination of Employment for any reason, Executive shall not, without the prior written consent of the Company, solicit or induce any then-existing employee of the Company or any of its subsidiaries to leave employment with the Company or any of its subsidiaries or contact any then-existing customer or vendor under contract with the Company or any of its subsidiaries for the purpose of obtaining business similar to that engaged in, or received (as appropriate), by the Company.

(d) Cooperation. Executive agrees that during the Employment Term or following a Termination of Employment for any reason, Executive shall, upon reasonable advance notice, assist and cooperate with the Company with regard to any investigation or litigation related to a matter or project in which Executive was involved during Executive’s employment. The Company shall reimburse Executive for all reasonable and necessary expenses related to Executive’s services under this Section 8(d) (i.e., travel, lodging, meals, telephone and overnight courier) within ten (10) business days of Executive submitting to the Company appropriate receipts and expense statements.

(e) Survivability. The duties and obligations of Executive pursuant to this Section 8 shall survive the termination of this Agreement and Executive’s Termination of Employment for any reason.

(f) Remedies. Executive acknowledges that the protections of the Company set forth in this Section 8 are fair and reasonable. Executive agrees that remedies at law for a breach or threatened breach of the provisions of this Section 8 would be inadequate and, therefore, the Company shall be entitled, in addition to any other available remedies, without posting a bond, to equitable relief in the form of specific performance, temporary restraining order, temporary or permanent injunction, or any other equitable remedy that may be then available.

(g) Limitation. If the duration, scope, or nature of any restriction on business activity covered by any provision of Section 8(b) or (c) above is in excess of what is valid and enforceable under applicable law, such restriction shall be construed to limit duration, scope or

activity to an extent that is valid and enforceable, with such extent to be the maximum extent possible under applicable law. For each of Section 8(b) and (c) above, Executive hereby acknowledges that such Section shall be given the construction which renders its provisions valid and enforceable to the maximum extent, not exceeding its express terms, possible under applicable law.

9. Miscellaneous.

(a) Resolution of Disputes and Reimbursement of Legal Costs. Except as otherwise provided in Section 8, the Company and Executive agree that any controversy or claim arising out of or relating to this Agreement or the breach thereof shall be settled by arbitration administered by the American Arbitration Association in accordance with its Commercial Arbitration Rules then in effect. Venue for any arbitration pursuant to this Agreement will lie in Louisville, Kentucky. Any award entered by the arbitrator(s) shall be final, binding and nonappealable and judgment may be entered thereon by either party in accordance with applicable law in any court of competent jurisdiction. This arbitration provision shall be specifically enforceable. Each party shall be responsible for its own expenses relating to the conduct of the arbitration (including reasonable attorneys' fees and expenses) and shall share the fees of the American Arbitration Association and the arbitrator(s), if applicable, equally.

(b) Governing Law. This Agreement will be governed by, and interpreted in accordance with, the laws of the Commonwealth of Kentucky applicable to agreements made and to be wholly performed within the Commonwealth of Kentucky, without regard to the conflict of laws provisions of any jurisdiction which would cause the application of any law other than that of the Commonwealth of Kentucky.

(c) Entire Agreement/Amendments. This Agreement contains the entire understanding of the parties with respect to the employment of Executive by the Company. There are no restrictions, agreements, promises, warranties, covenants or undertakings between the parties with respect to the subject matter herein other than those expressly set forth herein. This Agreement may not be altered, modified, or amended except by written instrument signed by the parties hereto. Sections 7 and 8 of this Agreement shall survive the termination of Executive's employment with the Company, except as otherwise specifically stated therein.

(d) Neutral Interpretation. This Agreement constitutes the product of the negotiation of the parties hereto and the enforcement of this Agreement shall be interpreted in a neutral manner, and not more strongly for or against any party based upon the source of the draftsmanship of the Agreement. Each party has been provided ample time and opportunity to review and negotiate the terms of this Agreement and consult with legal counsel regarding the Agreement.

(e) No Waiver. The failure of a party to insist upon strict adherence to any term of this Agreement on any occasion shall not be considered a waiver of such party's rights or deprive such party of the right thereafter to insist upon strict adherence to that term or any other term of this Agreement.

(f) Severability. In the event that any one or more of the provisions of this Agreement shall be or become invalid, illegal or unenforceable in any respect, the validity, legality and enforceability of the remaining provisions of this Agreement shall not be affected thereby.

(g) Successors.

(i) This Agreement is personal to Executive and shall not be assignable by Executive otherwise than by will or the laws of descent and distribution. This Agreement shall inure to the benefit of and be enforceable by Executive's legal representatives.

(ii) This Agreement shall inure to the benefit of and be binding upon the Company and its successors and assigns. The Company shall require any successor (whether direct or indirect, by purchase, merger, reorganization, consolidation, acquisition of property or stock, liquidation, or otherwise) to all or a substantial portion of its business and/or assets, by agreement in form and substance reasonably satisfactory to Executive, expressly to assume and agree to perform this Agreement in the same manner and to the same extent that the Company would be required to perform this Agreement if no such succession had taken place. Regardless of whether such an agreement is executed, this Agreement shall be binding upon any successor of the Company and such successor shall be deemed the "Company" for purposes of this Agreement.

(h) Notice. For the purpose of this Agreement, notices and all other communications provided for in this Agreement shall be in writing and shall be deemed to have been duly given if delivered personally, if delivered by overnight courier service, if sent by facsimile transmission or if mailed by United States registered mail, return receipt requested, postage prepaid, addressed to the respective addresses or sent via facsimile to the respective facsimile numbers, as the case may be, as set forth below, or to such other address as either party may have furnished to the other in writing in accordance herewith, except that notice of change of address shall be effective only upon receipt; provided, however, that (i) notices sent by personal delivery or overnight courier shall be deemed given when delivered; (ii) notices sent by facsimile transmission shall be deemed given upon the sender's receipt of confirmation of complete transmission, and (iii) notices sent by United States registered mail shall be deemed given two days after the date of deposit in the United States mail.

If to the Company, to:

Churchill Downs Incorporated  
Attn: General Counsel  
700 Central Avenue  
Louisville, KY 40208

With a copy to:

Vedder Price P.C.  
Attn: Michael A. Nemeroff, Esq.  
222 North LaSalle Street  
Chicago, IL 60601  
Facsimile: (312) 609-5005

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If to Executive, to such address as shall most currently appear on the records of the Company.

(i) Withholding. The Company may withhold from any amounts payable under this Agreement such Taxes (as defined in Section 10 (s)) as may be required to be withheld pursuant to any applicable law or regulation.

(j) Counterparts and Signatures. This Agreement may be signed in counterparts, each of which shall be an original, with the same effect as if the signatures thereto and hereto were upon the same instrument. Signatures delivered by facsimile or PDF file shall constitute original signatures.

(k) Code Section 409A. It is intended that any amounts payable under this Agreement and the Company's and Executive's exercise of authority or discretion hereunder shall comply with Code Section 409A (including the Treasury regulations and other published guidance relating thereto) so as not to subject Executive to the payment of any interest or additional tax imposed under Code Section 409A. To the extent any amount payable under this Agreement would trigger the additional tax imposed by Code Section 409A, the Agreement shall be modified to avoid such additional tax.

#### 10. Definitions.

(a) "Agreement" – see the recitals to this Agreement.

(b) "Base Salary" – see Section 3.

(c) "Board" means the Board of Directors of the Company.

(d) "Cause" for termination by the Company of Executive's employment with the Company means any of the following:

(i) the willful and continued failure of Executive to perform substantially his duties to the Company (other than any such failure resulting from incapacity due to disability), after a written demand to cure such failure (the "Demand to Cure") is delivered to Executive by the Chairman of the Board which specifically identifies the manner in which the Board believes that Executive has not substantially performed his duties;

(ii) Executive's conviction of, or plea of guilty or no contest to (A) a felony or (B) a misdemeanor involving dishonesty or moral turpitude; or

(iii) the willful engaging by Executive in illegal conduct or gross misconduct which is materially and demonstrably injurious to the business or reputation of the Company.

For purposes of this definition, no act or failure to act, on the part of Executive, shall be considered "willful" unless it is done, or omitted to be done, by Executive in bad faith or without reasonable belief that Executive's action or omission was in the best interests of the Company. Any act, or failure to act, based upon specific authority given pursuant to a resolution duly adopted by the Board or upon instructions of the Chairman of the Board or based upon the advice of counsel of the Company which Executive honestly believes is within such counsel's

competence shall be conclusively presumed to be done, or omitted to be done, by Executive in good faith and in the best interests of the Company. The Company shall give written notice to Executive of the termination for Cause. Such notice shall state in detail the particular act or acts or the failure or failures to act that constitute the grounds on which the Cause termination is based and such notice shall be given within six (6) months of the occurrence of, or, if later, the Company's actual knowledge of, the act or acts or the failure or failures to act which constitute the grounds for Cause. Executive shall have sixty (60) days upon receipt of the Demand to Cure in which to cure such conduct, to the extent such cure is possible.

(e) "Change in Control" means the first to occur of the following events:

(i) the acquisition, directly or indirectly, by any individual, entity or group (within the meaning of Section 13(d)(3) or 14(d)(2) of the Securities Exchange Act of 1934 (the "Exchange Act") (a "Person") of beneficial ownership (within the meaning of Rule 13d-3 promulgated under the Exchange Act) of more than 50% of either the then outstanding voting securities of the Company (the "Outstanding Company Common Stock") or the combined voting power of the then outstanding voting securities of the Company entitled to vote generally in the election of directors (the "Outstanding Company Voting Securities"); provided, however that for purposes of this subsection (i), the following acquisitions shall not constitute a Change in Control: (w) any acquisition directly from the Company, (x) any acquisition by the Company or any of its subsidiaries, (y) any acquisition by any employee benefit plan (or related trust) sponsored or maintained by the Company or any corporation controlled by the Company, or (z) any acquisition by any corporation pursuant to a transaction which complies with clauses (A), (B) and (C) of subsection (iii) of this definition;

(ii) individuals who, as of the Effective Date, constitute the Board (the "Incumbent Board") cease for any reason to constitute at least a majority of the Board; provided, however, that any individual becoming a director subsequent to the Effective Date whose election, or nomination for election by the Company's shareholders, was approved by a vote of at least a majority of the directors then comprising the Incumbent Board shall be considered as though such individual were a member of the Incumbent Board, but excluding, for this purpose, any such individual whose initial assumption of office occurs as a result of an actual or threatened election contest with respect to the election or removal of directors or other actual or threatened solicitation of proxies or consents by or on behalf of a Person other than the Board;

(iii) consummation of a reorganization, merger or consolidation or sale or other disposition of all or substantially all of the assets of the Company or the acquisition of assets of another entity (a "Corporate Transaction"), in each case, unless, immediately following such Corporate Transaction, (A) all or substantially all of the individuals and entities who were the beneficial owners, respectively, of the Outstanding Company Common Stock and Outstanding Company Voting Securities immediately prior to such Corporate Transaction beneficially own, directly or indirectly, more than 50% of, respectively, the then-outstanding shares of common stock and the combined voting power of the then-outstanding voting securities entitled to vote generally in the election of directors, as the case may be, of the corporation resulting from such Corporate Transaction (including, without limitation, an entity which as a result of such transaction owns the Company or all or substantially all of the Company's assets either directly or through one or more subsidiaries) in substantially the same proportions as their ownership, immediately prior to such Corporate Transaction, of the Outstanding Company Common Stock and Outstanding Company Voting Securities, as the case may be, (B) no Person

(excluding any corporation resulting from such Corporate Transaction or employee benefit plan (or related trust) of the Company or such corporation resulting from such Corporate Transaction) beneficially owns, directly or indirectly, 50% or more of, respectively, the then-Outstanding Company Common Stock resulting from such Corporate Transaction or the Outstanding Company Voting Securities resulting from such Corporate Transaction, except to the extent that such ownership existed prior to the Corporate Transaction, and (C) at least a majority of the members of the Board resulting from the Corporate Transaction were members of the Incumbent Board at the time of the execution of the initial plan or action of the Board providing for such Corporate Transaction; or

(iv) approval by the shareholders of the Company of a complete liquidation or dissolution of the Company.

(f) “Code” means the Internal Revenue Code of 1986, as amended from time-to-time.

(g) “Common Stock” means the common stock, no par value, of the Company.

(h) “Company” – see the recitals to this Agreement.

(i) “Disability” means that Executive becomes “disabled” within the meaning of Section 409A(a)(2)(C) of the Code or any successor provision and the applicable regulations thereunder.

(j) “Employment Term” – see Section 1.

(k) “Exchange Act” means the Securities Exchange Act of 1934.

(l) “Executive” – see recitals to this Agreement.

(m) “Fair Market Value” means, as of any date, (i) the closing price of the Common Stock on such date reported on The NASDAQ Stock Market (or, if no sale of the Common Stock was reported for such date, on the next preceding date on which such a sale of such security was reported), (ii) if the Common Stock is not listed on The NASDAQ Stock Market, but is listed on a national securities exchange, the closing price of the Common Stock on such date reported by such exchange, (or, if no sale of the Common Stock was reported for such date, on the next preceding date on which such a sale of such security was reported), (iii) if the Common Stock is not listed on The NASDAQ Stock Market or any national securities exchange, the average of the high bid and low asked quotations for the Common Stock on such date in the over-the-counter market (or, if no quotation of the Common Stock was reported for such date, on the next preceding date on which such quotation of such security was reported), or (iv) if there is no public market for the Common Stock, the fair market value of the Common Stock determined by the Board in good faith exercise of its discretion; provided, however, such determination shall be made in a manner consistent with Code Section 409A and official guidance thereunder.

(n) “ Good Reason ” for termination by Executive of Executive’s employment means the occurrence (without Executive’s express written consent) of any one of the following acts by the Company or failures by the Company to act:

(i) the assignment to Executive of any duties inconsistent in any material respect with the position of President and Chief Executive Officer (including status, office, title and reporting requirements), or the authority, duties or responsibilities of the President and Chief Executive Officer, or any other diminution in any material respect in such position, authority, duties or responsibilities unless agreed to by Executive;

(ii) the Company’s requiring Executive to be based at, or perform his principal functions at, any office or location other than a location within 35 miles of the Main Office unless such other location is closer to Executive’s then-primary residence than the Main Office;

(iii) a reduction in Base Salary;

(iv) a reduction in Executive’s welfare benefits plans, qualified retirement plan, or paid time off benefit unless other senior executives suffer a comparable reduction;

(v) any purported termination of Executive’s employment under this Agreement by the Company other than for Cause, death or Disability; and

(vi) the Company’s notice to Executive of non-renewal of the Agreement, or failure of the parties to reach mutually agreeable revised extension terms within 60 days following a party’s notice of non-renewal of the Agreement.

Prior to Executive’s right to terminate this Agreement, he shall give written notice to the Company of his intention to terminate his employment on account of a Good Reason. Such notice shall state in detail the particular act or acts or the failure or failures to act that constitute the grounds on which Executive’s Good Reason termination is based and such notice shall be given within six (6) months of the occurrence of the act or acts or the failure or failures to act which constitute the grounds for Good Reason. The Company shall have sixty (60) days upon receipt of the notice in which to cure such conduct, to the extent such cure is possible.

(o) “ Main Office ” means 700 Central Avenue, Louisville, Kentucky.

(p) “ Option ” means an option to purchase shares of Common Stock.

(q) “ Restricted Shares ” see Section 5(a).

(r) “ Restricted Stock Unit ” means the right to receive a share of Common Stock after a Termination of Employment, with such right subject to a risk of forfeiture or other restrictions that will lapse upon the achievement of one or more goals, such as the completion of service by Executive or achievement of certain performance objectives. Due to Code Section 409A, it is expected that any shares of Common Stock received per a Restricted Stock Unit shall be received six (6) months after a Termination of Employment.

(s) “ Taxes ” means the incremental United States federal, state and local income, excise and other taxes payable by Executive with respect to any applicable item of income.

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(t) “ Tax Gross-Up Payment ” means an amount payable to Executive such that, after payment of Taxes on such amount, there remains a balance sufficient to pay the Taxes being reimbursed, which amount shall be payable in a lump sum to Executive not later than the end of the taxable year of Executive next following the taxable year of Executive in which the related Taxes were remitted. The amount of Taxes eligible for reimbursement in one taxable year of Executive shall not affect the amount of Taxes eligible for reimbursement in another taxable year of Executive.

(u) “ Termination of Employment ” means a termination by the Company or by Executive of Executive’s employment with the Company.

11. Section 409A. Notwithstanding the foregoing, to the extent required in order to avoid accelerated taxation and/or tax penalties under Code Section 409A and the rules and regulations thereunder (“Section 409A”), if Executive is a “specified employee” (as defined under Section 409A) as of the date of his “separation from service” (as defined under Section 409) from the Company, then any payment of benefits scheduled to be paid by the Company to Executive during the first six (6) month period following the date of a termination of employment hereunder shall not be paid until the earlier of (a) the expiration of the six (6) month period measured from the date of Executive’s “separation from service” and (b) the date of Executive’s death. All payments and benefits that are delayed pursuant to the immediately preceding sentence shall be paid to Executive in a lump sum as soon as practicable following the expiration of such period (or if earlier, upon Executive’s death) but in no event later than thirty (30) days following such period. To the extent required in order to avoid accelerated taxation and/or tax penalties under Section 409A, no amount or benefit that is payable upon a termination of employment or services from the Company shall be payable unless such termination also meets the requirements of a “separation from service” under Section 409A. In addition, the parties shall cooperate fully with one another to ensure compliance with Section 409A, including, without limitation, adopting amendments to arrangements subject to Section 409A and operating such arrangements in compliance with Section 409A.

*[Signature page follows.]*

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**IN WITNESS WHEREOF** , the parties hereto have duly executed this Agreement as of the day and year first above written.

**ROBERT L. EVANS**

/s/ Robert L. Evans

**CHURCHILL DOWNS INCORPORATED**

By: /s/ Leonard S. Coleman, Jr.

Leonard S. Coleman, Jr.  
Chairman, Compensation Committee  
of the Board of Directors

## CERTIFICATION OF CHIEF EXECUTIVE OFFICER

I, Robert L. Evans, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Churchill Downs Incorporated;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 3, 2010

/s/ Robert L. Evans

Robert L. Evans  
President and Chief Executive Officer  
(Principal Executive Officer)

**CERTIFICATION OF CHIEF FINANCIAL OFFICER**

I, William E. Mudd, certify that:

1. I have reviewed this Quarterly Report on Form 10-Q of Churchill Downs Incorporated;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: November 3, 2010

/s/ William E. Mudd

William E. Mudd  
Executive Vice President and Chief Financial Officer  
(Principal Financial Officer)

**Certification of CEO and Chief Financial Officer Pursuant to  
18 U.S.C. Section 1350,  
As Adopted Pursuant to  
Section 906 of the Sarbanes-Oxley Act of 2002**

In connection with the Quarterly Report on Form 10-Q of Churchill Downs Incorporated (the "Company") for the quarterly period ended September 30, 2010 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), Robert L. Evans, as President and Chief Executive Officer (Principal Executive Officer) of the Company, and William E. Mudd, as Executive Vice President and Chief Financial Officer (Principal Financial Officer) of the Company, each hereby certifies, pursuant to 18 U.S.C. § 1350, as adopted pursuant to § 906 of the Sarbanes-Oxley Act of 2002, to the best of his knowledge, that:

- (1) The Report fully complies with the requirements of section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Robert L. Evans

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Robert L. Evans  
President and Chief Executive Officer  
(Principal Executive Officer)  
November 3, 2010

/s/ William E. Mudd

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William E. Mudd  
Executive Vice President and Chief Financial Officer  
(Principal Financial Officer)  
November 3, 2010

This certification is being furnished to the Securities and Exchange Commission as an exhibit to the Report and shall not be deemed filed by the Company for purposes of § 18 of the Securities Exchange Act of 1934, as amended.

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to Churchill Downs Incorporated and will be retained by Churchill Downs Incorporated and furnished to the Securities and Exchange Commission or its staff upon request.