



STATE REGULATION OF FANTASY SPORTS NOW APPEARS INEVITABLE: HOW AND BY WHICH AGENCIES SHOULD IT BE REGULATED?

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INTRODUCTION: WHERE WE ARE AND HOW WE GOT HERE

Before October, 2015, the major daily fantasy sports (“DFS”) operators accepted players in their pay-to-play contests from all U.S. states except five: Arizona, Iowa, Louisiana, Montana and Washington. On October 5, 2015, it was reported that some of their employees were winning large jackpots playing on rival sites.¹ Since then, several states have investigated DFS operations, and ten attorneys general have issued statements or formal opinions relating to the conduct of fantasy sports contests in their states: Georgia, Hawaii, Illinois, Maryland, Massachusetts, Mississippi, Nevada, New York, Rhode Island and Texas.² All except three concluded that DFS contests constituted gambling under applicable state law, and thus were unlawful, or, in the case of Nevada, unlawful unless licensed. The attorneys general in Maryland, Massachusetts and Rhode Island were the exceptions. The Maryland Attorney General opined that a 2012 Maryland law³ purporting to legalize fantasy sports contests in that state actually may have legalized only season-long contests, and that to the extent the law purported to legalize daily contests, it may have been an expansion of gambling which should have been subject to a state-wide voter referendum.⁴ Rhode Island Attorney General Peter Kilmartin opined that DFS contests operating in that state were not violating Rhode Island’s gambling laws,⁵ and in Massachusetts, although she issued no formal opinion on the issue, Attorney General Maura Healey stated that paid fantasy sports tournaments do not violate any federal or Massachusetts laws.⁶ Attor-

ney General Healey has since issued draft regulations that would protect fantasy sports players, and those regulations have yet to become final.

In response to these opinions and investigations, DFS operators have curtailed their operations, decreasing the number of states in which paid contests with prizes are offered. For example, FanDuel and DraftKings no longer allow players in Hawaii, Mississippi and Nevada (in addition to the original five) to compete for prizes, four other DFS operators have taken similar action with respect to Florida, Vermont and New York, and a smaller number no longer allow players in Arkansas and Tennessee to compete for prizes.⁷ Star Fantasy Leagues no longer accepts paying players from all but 21 U.S. states, and StarDraft—owned by casino supplier and PokerStars owner Amaya—no longer accepts players from all but four U.S. states, likely to avoid jeopardizing its existing (and unrelated) gaming licenses.⁸

Against this backdrop, as of March, 2016, at least thirty-one states have proposed legislation that would clarify the status of fantasy sports contests. This includes Virginia, which on March 7, 2016 enacted a law legalizing and regulating fantasy sports contests. (In addition, in May, 2015, Kansas enacted a law that legalized fantasy sports contests by removing them from the scope of the term “bet,” as used in Kansas’ gambling laws.) Most of the pending bills would establish that fantasy sports contests do not constitute gambling under applicable state laws, and several would regulate such contests, calling for fantasy sports operators to implement certain player protec-

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1 See: http://espn.go.com/chalk/story/_/id/13825667/new-york-attorney-general-eric-schneiderman-launches-inquiry-draftkings-fanduel and <http://www.nytimes.com/2015/10/06/sports/fanduel-draftkings-fantasy-employees-bet-rivals.html>, last accessed March 12, 2016.

2 Note also that Rick Kalm, Executive Director of the Michigan Gaming Control Board is reported as having told GamblingCompliance online magazine: “We here at the Michigan Gaming Control Board believe fantasy sports daily wagering to be illegal under Michigan Law.” See: http://gamblingcompliance.com/premium-content/news_analysis/daily-fantasy-sports-illegal-says-michigan-regulator, last accessed March 14, 2016.

3 2012 Md. Laws, ch. 346.

4 Letter dated January 15, 2016 to The Honorable Thomas V. Mike Miller, Jr.

5 Letter dated February 4, 2016, to Governor Gina Raimondo, Senate President M. Teresa Paiva Weed and Speaker of the House Nicholas A. Mattiello.

6 See <http://www.legalsportsreport.com/4800/massachusetts-daily-fantasy-sports-deveopments/>, last accessed March 12, 2016.

7 See: <http://www.legalsportsreport.com/daily-fantasy-sports-blocked-allowed-states/>, last accessed March 6, 2016.

8 Id.

tions—e.g., placing player funds in escrow, prohibiting operator employees from competing in their own or rival DFS contests, providing certain disclosures and allowing for self-exclusion. Some pending laws would require that operators be licensed while others, like the new Virginia law, would require only that they register with a state agency. Most would assess a license or registration fee, while others would also tax the operators' profits.

PENDING FANTASY SPORTS LEGISLATION ACROSS THE STATES

Pursuant to bills pending in seven states, fantasy sports contests would be made legal and regulatory authority over operators would be given to the state attorney general. (See the chart below.) Under bills in other states, the contests would be legalized and regulatory oversight would be given to different state agencies, in many cases agencies—like the attorney general—responsible for the protection of consumers. Only in a few cases—i.e., in bills pending in Florida, Illinois, Maryland, Minnesota, New Jersey, New York, Rhode Island—would the agencies charged with regulating fantasy sports operators also be the primary regulators of gambling facilities.

Fantasy sports operators seem to have accepted that government regulation of their industry is inevitable, and such regulation so far is emphasizing consumer protection. DFS operators and the Fantasy Sports Trade Association (“FSTA”) now routinely praise state legislation that establishes the legality of paid DFS contests, even though it imposes regulatory burdens and costs.

Questions facing state legislators seeking to legalize and regulate fantasy sports

Ultimately, the critical questions facing legislators seeking to allow paid fantasy sports contests and at the same time protect players are:

1. Should fantasy sports operators be licensed, as opposed to merely registered or subject to regulation? That is, how “heavy” a regulatory infrastructure is desired?
2. If fantasy sports operators are to be licensed or registered:
 - A. To what extent, if at all, should other participants be required to be licensed or registered—e.g., should providers of software, equipment and/or services, and their employees, also be licensed or registered?
 - B. To what extent should entities subject to licensing be investigated? That is, what is the appropriate intensity level of the investigation, if any?
 - C. What criteria should be used to determine whether a license should be granted (e.g., honesty, criminal record, licensing history, financial soundness and ability to perform)?
3. What player protections are appropriate? More specifically, what protections are appropriate to ensure that (i) fantasy sports contests are run honestly and without collusion, (ii) the contests are fair, in that players are compete on an equal basis, (iii) the contests are run transparently, such that players understand their likelihood of winning, (iv) player funds are protected from loss by operators, (v) player confidential information is protected, and (vi) underage and problem gaming is addressed?
4. Are additional measures needed to address money laundering?
5. Should DFS contests be regulated dif-

ferently than the season-long variety? Should the season-long variety be regulated at all?

6. Should raising revenue be among the goals of fantasy sports regulation?

The answers to these questions will vary by state, as each state legislature knows best the sensibilities of its citizens. However, legislatures contemplating fantasy sports legislation should consider the significant differences between fantasy sports contests and online gambling and consider—as the evidence suggests many are—that the regulation appropriate for online gambling may not be appropriate for fantasy sports.

A “heavy” regulatory licensing infrastructure, such as applied to online gambling in the states in which it exists, is probably not appropriate or necessary for fantasy sports given the significant differences between the businesses. Online gambling involving slots and other house-banked games operate on a different (and so far apparently more profitable) business model than fantasy sports tournaments. In slots, lotteries and other house-banked games, winners are determined by a deal of the cards or a random event (e.g., a random number generator or a draw machine). The operator has control over the random event, and thus there exists the potential for the operator to “fix” the outcome. In fantasy sports, the outcome of the contest depends upon the skill of the participants in selecting their lineups, which skill is then reflected by the collective performances of the athletes in the lineups selected, measured by the applicable contest scoring system.⁹ Each of these events—the lineup selection and the performance of the selected athletes—is outside the control of the operator. Even if a house-banked game operates exactly as it should, the odds of winning are set such that the house is certain

9 In fantasy sports contests, the evidence shows that player skill rather than chance determines the outcome. See <http://www.bloomberg.com/news/articles/2015-09-10/you-aren-t-good-enough-to-win-money-playing-daily-fantasy-football>, last accessed March 13, 2016. This is in contrast to

sports-betting, in which players pick teams against a “spread” set by Nevada odds-makers. Such has been held to be a game of chance. *National Football League v. Delaware Lottery*, 435 F.Supp. 1372 (D. Del. 1977).

State	Pending State Legislation	Proposed State Body to Regulate Legal Fantasy Sports Contests
Alabama	H. 56	Attorney General
Arizona	S. 1515	Attorney General
California	A. 1437	Attorney General
Connecticut	S. 192	Commissioner of Consumer Protection
Florida	H. 707 and S. 832	Department of Business and Professional Regulation
Georgia	S. 352	Attorney General
Hawaii	H. 1838 and S. 2722 (two other pending bills would declare paid fantasy sports gambling and thus unlawful)	Attorney General
Illinois	H. 4323 and S. 2193 S. 2843	Attorney General Gaming Board
Indiana	S. 339	Gaming Commission
Iowa	S. 166, H. 47 and S.1068	These bills would make fantasy sports contests lawful contests of skill without establishing regulatory oversight.
Kentucky	H. 625	Public Protection Cabinet
Louisiana	H. 676	This bill would exempt fantasy sports from the state law definitions of “gambling” and “gambling by computer”
Maryland	S. 976 and H. 930 S. 980	Lottery and Gaming Control Commission This bill would legalize certain fantasy sports contests, but make clear that on-line fantasy sports contests are unlawful.
Massachusetts	S. 191 Regulations proposed by the Attorney General – 940 C.M.R. 34.00 (proposed)	This bill would authorize and direct the Lottery to conduct online games of skill, including but not limited to fantasy sports contests. These regulations – proposed pursuant to the Attorney General’s existing authority – would require the implementation of various consumer protections by fantasy sports operators.
Michigan	S. 459	This bill would exempt fantasy sports from the state’s criminal gambling laws.
Minnesota	H. 2426	Commissioner of Public Safety
Mississippi	S. 2541	Commissioner of Insurance
Missouri	H. 2941 and S. 1041	Department of Insurance, Financial Institutions and Profession Registration
Nebraska	L. 862	This bill would exempt fantasy sports from the state’s gambling laws.
New Jersey	S. 1927	Department of Law and Public Safety
New Mexico	H. 314	Secretary of State
New York	S. 6793 A. 8554 and S. 6305	Department of Financial Services Gaming Commission
Oklahoma	H. 2278 and S. 1396	Department of Consumer Credit
Rhode Island	H. 7075, H. 7492, 7917 and 7938	Department of Business Regulation, Division of Racing and Athletics
South Carolina	S. 1093	Department of Consumer Affairs
Tennessee	H. 2254 and S. 2151 H. 2105 and S. 2109	Would establish an advisory task force to review games of skill, including fantasy sports contests. Would establish an advisory task force to review online simulated competitions, including fantasy sports contests.
Vermont	S. 223	Attorney General
Virginia	S. 646	This bill became law March 7, 2016. It calls for registration and regulation of fantasy sports operators by the Department of Agriculture and Consumer Services.
Washington	S. 5284, H. 1301 and S. 6333 H. 2370	Each of these bills would classify fantasy sports contests as contests of skill and therefore not “gambling” under applicable state law. This bill would deem fantasy sports contests to be games of chance and would prohibit paid fantasy sports contests.
West Virginia	S. 529 and H. 4583	This bill would exempt fantasy sports contests from the state’s gambling laws.
Wisconsin	A. 800 and S. 702	Department of Financial Institutions

to win over time, and the house earns, in general, a fixed percentage of the gross gaming revenue.¹⁰ In fantasy sports by contrast, the operator acts somewhat like an agent for the players, shifting money from losers to winners and taking out a fee—generally around ten percent of the total entry fees. Thus, online gaming presents a greater profit potential and, arguably, a greater potential¹¹ for corruption than fantasy sports. In regard to fantasy sports, it seems appropriate that the regulatory focus be on making the games fair and transparent.¹²

Similarly, legislators should consider whether it is appropriate to impose the same regulatory burdens on season-long fantasy sports contests that they impose on DFS contests.¹³ For example, Virginia's newly-enacted law and Indiana's pending bill require the same \$50,000 registration fee from season-long contest operators as is required from daily contest operators, without regard to total contest entry fees.¹⁴ This may drive season-long operators from the state (unless they also operate established daily fantasy games). This would be ironic, since the concerns attorneys general have had with fantasy sports have related almost exclusively to the daily variety. In his letter seeking to halt the operations of DFS operators FanDuel and DraftKings, New York Attorney General Eric Schneiderman contrasted daily fantasy sports contests with the season-long variety and

stated that the latter was an activity “enjoyed and legally played by millions of New York residents.”¹⁵

COMMON GROUND: PLAYER PROTECTION

One aspect of fantasy sports regulation about which there seems to be general agreement is the need for reasonable player protection. The recently-enacted Virginia fantasy sports law provides that, as a condition of registration, a fantasy sports operator must implement procedures that, among other things:

1. prevent the operator or his employees and relatives living in the same household from competing in any fantasy contest offered by such operator in which the operator offers a cash prize;
2. prevent the sharing with third parties of confidential information that could affect fantasy contest play until the information is made publicly available;
3. verify that any fantasy contest player is 18 years of age or older;
4. ensure that the athletes who are the subject of a fantasy contest are restricted from entering a fantasy contest that is determined, in whole or part, on the accumulated statistical results of a team of individuals in which such athletes are participants;
5. allow individuals to restrict themselves

from entering a fantasy contest upon request and take reasonable steps to prevent those individuals from entering the operator's fantasy contests;

6. disclose the number of entries a single fantasy contest player may submit to each fantasy contest and take reasonable steps to prevent such players from submitting more than the allowable number; and
7. segregate player funds from operational funds in separate accounts and maintain a reserve in the form of cash, cash equivalents, irrevocable letter of credit, bond, or a combination thereof in an amount sufficient to pay all prizes and awards offered to winning participants.

The Virginia law does not appear to require an investigation of operators seeking to be registered, although specific criteria for registration have yet to be established. The law provides that the Department of Agriculture and Consumer Services “shall issue” a registration to an applicant that meets the criteria to be established by the Department and has not committed any of certain specified bad acts.¹⁶

By contrast, the draft regulations proposed by the Massachusetts Attorney General contain the above consumer protections, but go further. If they become final, they will require DFS operators to:

10 According to federal regulations relating to Indian Gaming at 25 CFR 502.11, a house banked game means “any game of chance that is played with the house as a participant in the game, where the house takes on all players, collects from all losers, and pays all winners, and the house can win.”

11 Although the financial situations of fantasy sports operators are not public (as none is yet publicly traded), *Fortune* magazine reported on October 6, 2015 that neither FanDuel nor DraftKings was profitable. <http://fortune.com/2015/10/06/draftkings-fanduel-merger/>, (last accessed March 12, 2016). Their business prospects have become more uncertain since then. Indeed, in a February 9, 2016 article, it was reported that Twenty-First Century Fox Inc. had “marked down the value of its \$160 million investment in DraftKings Inc. by about 60 percent amid increasing challenges to the legality of daily fantasy sports contests.” See <https://www.bostonglobe.com/business/2016/02/09/fox-cuts-value-draftkings-stake-percent/0RCLppU4LkDreMyUVqZhKJ/story.html>, last accessed March 12, 2016.

12 The allegations of wrongdoing facing the fantasy sports industry consist mainly of claims that employees of operators used information not available to all players – i.e., “inside information” – and thus gaining an improper advantage, not “fixing” the outcome of contests. See http://www.nytimes.com/2015/10/12/sports/fantasy-sports-draftkings-fanduel-insiders-edge-football.html?_r=0, last accessed March 13, 2016.

13 Note that the number of season-long fantasy sports players dwarfs the number of players of the daily variety. The FSTA estimates that, in 2015, there were 46.2 million players of season-long fantasy sports and 8.9 million players of daily fantasy sports. See <http://www.slideshare.net/mayfairmobile/daily-fantasy-sports-miami-fl-august-2015-full-presentation-deck>, slide 10 of 261, last accessed March 12, 2016.

14 The newly-enacted Virginia law treats season-long fantasy sports the same as daily fantasy sports, although the latter are often conducted by hobbyists and involve considerably lower prizes. As a result, the \$50,000 registration fee may drive season-long contest operators from the market. Although the FSTA first praised the Virginia bill, after it was signed into law, the FSTA stated that it was “deeply concerned” at the “onerous mandatory regulation fee that makes [Virginia and Indiana, if the bill there is signed into law] untenable for the majority of the FSTA's members.” See <http://www.legalsportsreport.com/8915/fsta-pushes-back-on-dfs-fees/>, last accessed March 13, 2016.

15 Cease and desist order dated November 10, 2015, from the office of New York Attorney General Eric Schneiderman to DraftKings.

16 The specified “bad acts” include having been found guilty of any illegal, corrupt, or fraudulent act, practice, or conduct in connection with any fantasy contest, or having been convicted of a felony or any criminal offense involving dishonesty or breach of trust within the 10 years prior to the date of application for registration.

1. limit play of DFS contests to persons 21 years of age and older;
2. not offer DFS contests involving college, high school or student sporting events;
3. prohibit the use of “scripts”—i.e., a list of commands that a DFS-related computer program can execute to automate processes on a DFS contest platform (e.g., to create and manage lineups);
4. limit DFS players to only one account and only one user name;
5. take “commercially and technologically reasonable measures” to verify DFS players’ true identities and addresses;
6. prohibit DFS players from using proxy servers to enter any DFS platform;
7. prevent simultaneous log-ins on a single account;
8. abide by several advertising restrictions, including no depiction of persons under 21 or school or college settings, no endorsements by persons under 21 or by colleges or college athletes, and no advertisements targeted at persons under 21;
9. implement and publish procedures by which players can set self-imposed deposit limits or self-imposed loss limits; and
10. comply with federal and state requirements regarding data security.

THOUGHTS ON THE FUTURE

Heavily-regulated casinos and Nevada sportsbooks appear to view fantasy sports contests as gambling that should be regulated as such. Accordingly, they can be expected to lobby state representatives to require fantasy sports operators to submit to heavy “gambling-style” regulation. Casino operator MGM and Nevada sportsbook operator William Hill took this position very publicly in the months before the Nevada Attorney General issued his opinion that DFS contests constituted “sports

pools” and “gambling games” under Nevada law (and thus must be licensed in order to be offered in that state).¹⁷

Whether state legislatures will be swayed by such arguments is not clear. States legislatures in states which do not have gaming commissions regulating casinos or internet gaming (e.g., states having only pari-mutuel wagering and lotteries) will likely not be under the same pressure to treat fantasy sports operators with a heavy hand and may focus instead on consumer protection. At the same time, states with little or no gambling may prefer to ban paid fantasy sports contests entirely. For example, although Hawaii has a bill pending that would make legal and lightly regulate fantasy sports, it also has a bill pending that would make paid fantasy sports contests clearly illegal.

Further, states with small populations may follow substantially the regulatory structures adopted before them by states with large populations, and may engage in reciprocity allowing for an abbreviated licensing procedure if an operator is licensed in another jurisdiction and is in good standing in all jurisdictions in which it is licensed. This would seem to be a wise approach for small states wishing to legalize paid fantasy sports contests, because otherwise they may not represent revenue significant enough to attract fantasy sports operators. For example, after the Nevada Attorney General opined that DFS operators could operate paid contests there only after becoming licensed, almost all DFS operators exited the state. Presumably they decided that the burden and expense of becoming licensed under Nevada’s “heavy” regulatory structure was not worth the revenue Nevada’s 1.5 million residents represented. (Of course, another reason for their exit may have been that they considered it unlikely that they would be licensed in light of their opera-

tions in other states where the lawfulness of their operations was not clear.)

Finally, it will be interesting to see whether there is a challenge to any state fantasy sports legislation under the Professional and Amateur Sports Protection Act (the “PASPA”).¹⁸ The PASPA prohibits the operation of “a lottery, sweepstakes, or other betting, gambling, or wagering scheme based, directly or indirectly ... on one or more performances of [amateur or professional] athletes” in the games in which they participate, pursuant to a state law (e.g., a licensing and regulation scheme imposed by state statute).¹⁹ States wishing to legalize and regulate DFS contests will presumably make clear in their legislation (to the extent they deem it necessary) that DFS contests do not constitute “a lottery, sweepstakes, or other betting, gambling, or wagering scheme.” However, such state-law interpretations will not govern the interpretation of those terms in the federal PASPA. Enforcement of the PASPA is left to the professional and amateur sports leagues whose games are involved, as well as the U.S. Attorney General, and the professional sports leagues presumably will be reluctant to bring a PASPA challenge given the benefits they receive from DFS contests—e.g., greater fan interest and viewership, and greater advertising dollars. However, the NCAA and several major college athletic conferences have opposed the use of their games and athletes as the basis for DFS contests,²⁰ and therefore could decide to bring a PASPA challenge if their games or athletes are used as the basis for such contests pursuant to a state law.

In short, it will be another interesting year for fantasy sports, as the industry continues to take shape. ■

17 See <http://www.reviewjournal.com/business/casinos-gaming/gambling-or-game-skill-debate-swirls-over-fantasy-sports>, last accessed March 13, 2016.

18 28 U.S.C. 3701 et seq.

19 28 U.S.C. 3702.

20 See <http://www.nytimes.com/2015/10/21/sports/ncaa-distances-itself-from-daily-fantasy-websites.html>, last accessed March 13, 2016.