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Daily Fantasy Sports: Industry Trends, Legal and Regulatory Issues, and Policy Options

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Summary

Daily fantasy sports (DFS) companies, which operate online gaming platforms that allow players to assemble imaginary sports teams and compete in daily or weekly contests, function in a gray area of the law. The federal government does not license or regulate them. State governments have the main responsibility for regulating gaming activities that offer the prospect of monetary rewards, but a series of federal laws, most recently the Unlawful Internet Gambling Enforcement Act of 2006 (UIGEA; P.L. 109-347), may limit states' ability to oversee DFS. The 2006 law, however, was enacted at a time when only season-long fantasy sports existed. Whether Congress intended it to exempt DFS from state regulation is unclear.

Congress, multiple states, and law enforcement agencies have questioned the legality of the fledgling DFS industry, with a central focus on whether DFS contests are indeed games of skill (which would most likely make DFS legal) or chance (which would probably make DFS unlawful gambling). The legal status of DFS under state law directly affects whether DFS operators may be federally prosecuted under the Illegal Gambling Business Act (P.L. 91-452) and whether banks and payment processors could be held liable for violating UIGEA if they process monetary transactions related to daily fantasy sports. It is also possible that courts could determine that the Professional and Amateur Sports Protection Act (PASPA; P.L. 102-559) prohibits most state legislatures from authorizing or regulating DFS.

In 2015, more than a dozen states considered whether or not to allow DFS operators to offer their gaming activities to individuals located within their borders. Nevada has decided to require DFS operators to obtain a license from its state gaming commission. Other states are considering a similar approach, which could include wagering taxes akin to the ones casinos pay. If state lawmakers decide to treat DFS as gambling, and if the courts determine that status is consistent with federal law, DFS would be subject to regulations, licensing, consumer protection safeguards, and other mandates where states choose to impose and enforce them. In the absence of state regulation, there is no means of assuring customers' access to funds on deposit with DFS operators and of enforcing prohibitions on participation by underage gamers.

Despite the controversy that surrounds it, the DFS sector is relatively small. FanDuel and DraftKings, the two largest operators, and the roughly two dozen smaller DFS companies are estimated to have booked around $86 million in net revenue (receipts minus prizes) from DFS in 2014, a small fraction of the regulated gambling industry's net revenue. Nonetheless, a variety of sports teams and organizations and media companies have invested in the DFS industry, suggesting a potential for rapid expansion if the industry's legal status is clarified.

There are strong differences of opinion within the traditional gambling industry on DFS. Some land-based casino operators fear losing customers to DFS games, while other casino owners see it as a potential new revenue source allowing them to attract younger players. Some Indian tribes that operate casinos have expressed concern about the prospect that DFS could reduce their revenues, but many tribes have not weighed in. In some states, racinos (gambling venues located at racetracks) may lobby to offer DFS sports to help increase interest in horse racing; in other states, racino operators worry that DFS will divert potential bettors from their facilities. A few state lotteries are considering whether to offer online DFS games.

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Introduction

Daily fantasy sports (DFS), a form of online gaming in which players assemble imaginary teams that amass points based on how well individual players perform in real-life sporting events, operates in a gray area of the law. The DFS industry has not been regulated by the federal government, but the attorneys general of several states have claimed that DFS either violates state laws or is subject to state regulation.

Congressional action directly affecting the DFS industry dates back to a 2006 law, the Unlawful Internet Gambling Enforcement Act (UIGEA; P.L. 109-347), which outlaws illegal gambling using the Internet and bars banks, credit card firms, and other financial service providers from processing payments to companies offering "unlawful Internet gambling."[1] UIGEA defines "unlawful Internet gambling" as placing or receiving a bet or wager via the Internet where such bet or wager is unlawful under either federal or state law.[2] UIGEA provides an exemption to this prohibition for online participation in fantasy sports if the games have certain attributes including set prize pools, skill-based contests, and outcomes that do not depend solely on the performance of a single real-world team or player.[3] However, DFS contests did not exist at the time of UIGEA's enactment in 2006, and there is debate about whether DFS, as presently offered to consumers, falls within the law's fantasy sports "exemption." It is also possible that courts could determine that DFS is subject to a 1992 law, the Professional and Amateur Sports Protection Act (PASPA; P.L. 102-559), which bans sports betting in most states, and to various other federal and state gambling laws. This uncertainty has drawn the attention of Congress, with some Members proposing to reexamine the legal status of the industry.

DFS Basics

Fantasy sports began as a type of informal gambling among friends, in which participants composed imaginary teams of active professional baseball players and won or lost depending on their players' statistical performance over the course of a full baseball season. Fantasy baseball developed into more formal "rotisserie leagues" in the 1980s, with elaborate rules and scoring systems.[4] Daily fantasy sports essentially extends the fantasy concept to other sports, compresses season-long games into daily and weekly formats, and allows them to be played online among participants with no personal connection.

DFS online gaming offers players a variety of sport options (e.g., baseball, basketball, football, and hockey), performance metrics, and types of contests ranging from one-on-one competitions to games with large numbers of participants. The idea is for a player to assemble an imaginary team that amasses points based on how well each individual on a team performs in real-life games, as measured by statistics such as the number of passing yards gained in football, the number of hits in baseball, or the percentage of three-point field goal attempts that are successful in basketball. To add to the challenge, every DFS player is given a salary cap, requiring that the sum of the real-life salaries of the players on each team fall below a specified level.[5]

[1] 31 U.S.C. §5363; 18 U.S.C. §2.

[2] 31 U.S.C. §5362(10)(A).

[3] 31 U.S.C. §5362(1)(E)(ix).

[4] Ben McGrath, "Dream Teams," *The New Yorker*, April 13, 2015, http://www.newyorker.com/magazine/2015/04/13/dream-teams.

[5] Fantasy Sports Trade Association (FSTA), "Why Fantasy Sports is Not Gambling, Understanding a Game of Skill," (continued...)

Depending on the game the participant chooses to enter, the rewards for winning could range from a few dollars to a large amount in a guaranteed prize pool (GPP).[6] DFS companies assert that these rewards are earned as the result of a fantasy sports player's skill rather than being the result of luck or chance. The companies' websites describe their offerings as "contests" and "games" and avoid such words as "gambling" and "bet." As discussed further below, the determination of whether players' rewards are earned as a result of skill or of chance may be significant in establishing the legal status of DFS.

According to a study published in *Sports Business Journal*, "DFS affords a huge advantage to skilled players. In the first half of the 2015 MLB season, 91% of DFS player profits were won by just 1.3% of players."[7] A separate survey of DFS participants conducted by Eilers Research in summer 2015 found that 70% of contestants lost money.[8] These studies seem to suggest that the best players dominate everybody else because a certain amount of skill goes into putting together a winning daily fantasy lineup.

One of the attractions of DFS is that it can be played on a variety of communication devices at a time and place of the participant's choosing. A typical fantasy sports player is younger, better educated, and wealthier than the usual visitor to a casino. A typical player is a male around 30 years of age who is extremely interested in sports and has played in fantasy leagues for several years.[9] Many DFS participants formerly played online poker, which in the United States is now legal in only three states.[10] According to the Fantasy Sports Trade Association (FSTA), the industry's national trade group, DFS players spent an average of $257 on entry fees and league-related materials in 2015.[11]

DFS Companies

The two main DFS companies, FanDuel, founded in 2009, and DraftKings, launched in 2012, accounted for about 95% of the market's revenue in 2014, according to various estimates.[12] Both companies are privately held. Roughly two dozen other companies also offer daily fantasy sports.

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http://fsta.org/research/why-fantasy-sports-is-not-gambling/. According to Marc Edelman, an associate professor of law at Baruch College, Kevin Bonnet coined the term daily fantasy sports when he launched Fantasy Sports Live, a DFS operator, in 2007.

[6] The big money is in a GPP, which guarantees the amount of money that will be paid out to winners in advance of the contest starting. If the DFS operator does not secure enough entrants to cover the prizes, it must make up the difference between the prizes to be paid and the entry fees collected. This is known in the industry as the "overlay."

[7] Ed Miller and Daniel Singer, "For Daily Fantasy Sports Operators, The Curse of Too Much Skill," *Sports Business Journal*, July 15, 2015, http://www.sportsbusinessdaily.com/Journal/Issues/2015/07/27/Opinion/From-the-Field-of-Fantasy-Sports.aspx. Ed Miller is an expert in poker strategy, and Daniel Singer heads the sports and gaming practice of McKinsey & Company, a consulting firm.

[8] Adam Krejcik and Chris Gove, "Daily Fantasy Sports Industry Update," Eilers Research, November 2015, p. 12.

[9] Adam Krejcik, "Daily Fantasy Sports: The Future of U.S. Sports Wagering?," Eilers Research, October 16, 2014, p. 7.

[10] Tyson Wilson and Dan Frey, "Fantasy Sports Overview," Washington State Gambling Commission, November 12, 2015, p. 13, http://www.wsgc.wa.gov/agenda/2015/nov-fantasy-sports-overview.pdf.

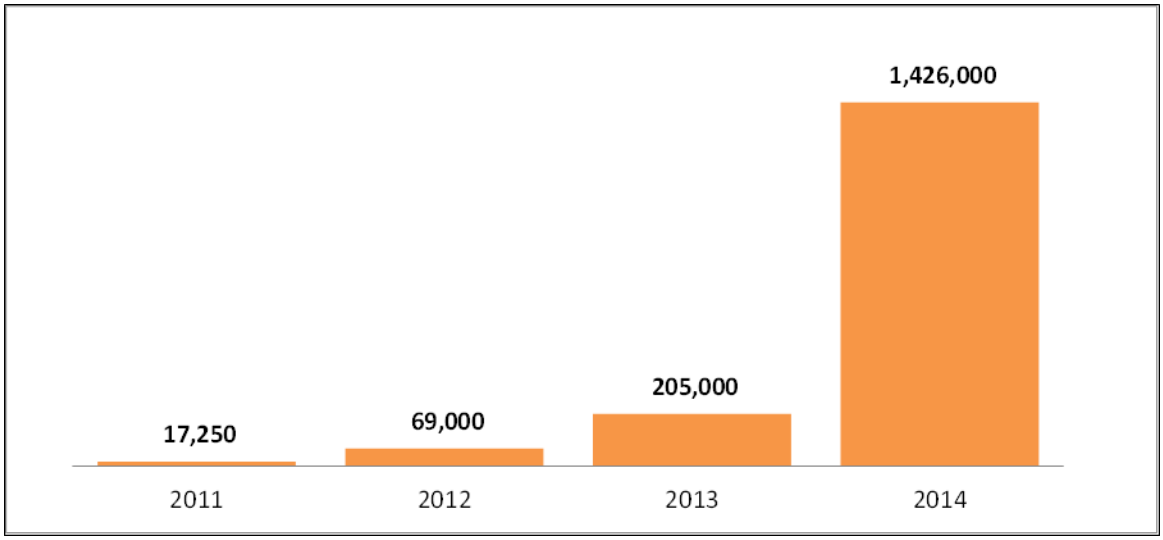
[11] FSTA, Industry Demographics, http://fsta.org/research/industry-demographics/.

[12] Adam Krejcik, "Keynote: Bold Predictions on the Daily Fantasy Sports Market," FSTA Winter Conference, January 16, 2014, p. 11, http://www.ifrahlaw.com/wp-content/uploads/2015/01/Eilers_Fantasy-Bold-Predictions-2015-FSTA-2.pdf.

The industry has a fairly simple revenue model. Players pay entry fees, which range from 25 cents to several thousand dollars, to compete in a single contest, whether against a small group of friends or against a huge pool of players seeking to win a prize pool in the millions of dollars. Operators in the industry typically keep a "rake" (the house's commission) of 5% to 15% of the total betting pool to cover operating costs and profit.[13] DFS companies claim to distribute the rest as winnings.

According to Eilers Research, which studies the gaming industry, the DFS industry's net revenue (entry fees minus prizes)[14] in the United States totaled $86 million in 2014. The research firm said in late 2014 that "none of the major DFS providers are generating a profit, and it's unlikely that anyone will be cash flow positive in the next two years."[15] Although DFS companies have not released detailed financial statements, it is generally believed that their aggressive advertising and marketing efforts are taking a large share of their net revenue.[16] As shown in **Figure 1**, FanDuel and DraftKings claim to have attracted 1.4 million paid active users in 2014, a huge uptick from fewer than 20,000 paid users as recently as 2011.[17] FSTA, however, claims that the number of DFS players is small compared to the nearly 60 million people it estimates to have played season-long fantasy sports in 2015.[18]

Figure 1. Paid Active DFS Users



Source: PrivCo data for FanDuel and DraftKings.

Note: Totals reflect paid active users on FanDuel's and DraftKings' websites.

[13] Rake is the amount of commission a DFS operator keeps from each entry fee as revenue for its operations. Rakes can vary by site and contest, but reportedly the typical rake is around 10% of the contest entry fees.

[14] DFS entry fees totaled an estimated $1 billion in 2015, and by some estimates they could reach $18 billion by 2020.

[15] Adam Krejcik, "Daily Fantasy Sports: The Future of U.S. Sports Wagering?," Eilers Research, October 16, 2014, pp. 3, 10.

[16] Ray Paulick, "Fantasy Sports: Horse Racing's Newest Threat," *The Paulick Report*, September 16, 2015, p. 5, http://www.paulickreport.com/wp-content/uploads/2015/09/KeeSept2c.pdf.

[17] PrivCo, *FanDuel*, p. 8, February 2, 2016, and PrivCo, *DraftKings*, p. 8, January 4, 2016.

[18] FSTA, Industry Demographics, http://fsta.org/research/industry-demographics/.

The major DFS operators are backed financially by investors with other sports-related interests. Investors in FanDuel include Turner Sports (a subsidiary of Turner Broadcasting System), and cable television distributors Time Warner Cable and Comcast, while investors and marketing partnerships in DraftKings include the Kraft Group (which owns the New England Patriots football team), the Fox Sports cable television network, and Major League Baseball.[19] In some cases, these investors may be less interested in the profitability of DFS than in its potential to enlarge the customer base for sports events and broadcasts. Sports leagues and associations have strongly opposed legalized sports betting, but some have supported the growth of fantasy sports partly because of the increased viewership that results from DFS contests.[20] Cable television companies that carry sports programming, in some cases on high-cost tiers of service or on a pay-per-view basis, may see a similar benefit. According to DFS operator FanDuel, fans consume 40% more sports content once they start playing daily fantasy sports.[21]

Other companies have entered the market. Yahoo!, a recent entrant into the DFS market, offers daily and weekly fantasy sports games played for cash prizes on the Yahoo Sports daily fantasy website.[22] CBS, the parent of the CBS television network, launched its own DFS product in August 2015.[23] The ESPN cable sports network has arranged for DraftKings to promote its programs during its programming, and vice versa, instead of launching its own DFS platform. Television network executives may be especially interested in the prospect that DFS may keep players tuned in to a game with a lopsided score because they are more interested in individuals' performance than the final outcome. Such ventures have the potential to change the structure of the DFS market considerably.

DFS and the Broader Gambling Industry

DFS is tiny relative to the gambling industry, whose casinos, Indian gaming operations, racinos, and state lotteries generated nearly $70 billion in net revenue in 2014.[24] Despite the DFS industry's modest size, its rapid growth has raised questions about its potential effect on the more established gambling industry. Casinos and casino hotels employed about 400,000 people nationwide in 2014,[25] and they are a major source of government revenue. Lotteries and taxes on commercial casinos and other types of gambling generated $27.3 billion for state governments in 2014, according to the Rockefeller Institute of Government of the State University of New York.[26]

[19] "MLB May End DraftKings Marketing Agreement Due to NY Law," *Sports Illustrated*, February 5, 2016, http://www.si.com/mlb/2016/02/05/mlb-daily-fantasy-sports-draftkings-marketing-agreement.

[20] Dustin Gouker, "What the NFL, NBA, and MLB Have to Say About Daily Fantasy Sports and Sports Betting," *Legal Sports Report*, November 4, 2015, http://www.legalsportsreport.com/5798/nfl-nba-mlb-on-dfs-and-sports-betting/.

[21] Jason Blake and Whitney Fishman Zember, *Spotlight on Fantasy Sports*, MEC, May 2015, p. 11, http://www.mecglobal.com/assets/publications/2015-06/SpotlightOn-FantasySports-May2015FINAL1.pdf.

[22] Yahoo!, "Yahoo Launches Yahoo Sports Daily Fantasy," press release, July 8, 2015, https://investor.yahoo.net/releasedetail.cfm?releaseid=921213.

[23] Dustin Gouker, "An Eye on DFS: CBS Launches Its Own Daily Fantasy Sports Product," *Legal Sports Report*, August 3, 2015, http://www.legalsportsreport.com/2848/cbs-sportsline-launches-daily-fantasy-sports/.

[24] University of Nevada, Las Vegas (UNLV), Center for Gaming Research, *United States Commercial Casino Revenues*, 2001-2014, July 2015, p. 1, http://gaming.unlv.edu/reports/national_annual_revenues.pdf. The North American Association of State & Provincial Lotteries (NASPL) provided data on gross gaming revenues generated from lottery sales to CRS by email.

[25] Bureau of Labor Statistics (BLS), Quarterly Census of Employment and Wages, NAICS 7132 and 72112, accessed January 6, 2016, http://www.bls.gov/cew/.

[26] Lucy Dadayan, *State Revenues from Gambling Show Weakness Despite Gambling Expansion*, The Nelson A. Rockefeller Institute of Government, March 23, 2015, p. 3.

In Nevada, gaming taxes made up about 24% of the state's general fund revenue in FY2014,[27] and Nevada counties collected additional fees and levies from casinos. Pennsylvania collects a tax of 55 cents on every dollar bet on slot machines in the state.[28] DFS companies historically have not been regulated as gambling in most states; however, the question of whether they should be is currently being litigated in a number of jurisdictions, as discussed in the "Legal Status and Regulatory Environment" section of this report.

Industry Positions on DFS Gaming

The traditional gambling industry itself is split on how to respond to DFS. Some land-based casino operators fear losing customers to DFS operators, as DFS players can now participate in contests from any spot outside a casino using their computers and mobile devices, and worry that DFS, especially if left unregulated, could become as disruptive to gambling as other Internet-based companies, such as Airbnb and Uber, have been to the hotel and taxi industries, respectively. Other gambling companies, however, see DFS as a possible way to tap into and introduce a younger generation generally unenthusiastic about bricks-and-mortar gambling to traditional gaming options such as slot machines and horse races. They see DFS as a possible new source of revenue, and a promising way to cross-market to individuals who might not otherwise enter a casino.[29]

This split is repeated within individual segments of the industry. For example, in Indiana, some racinos, which are gambling venues located at racetracks, want to offer DFS sports contests at licensed racetrack casinos in hopes of stimulating interest in horse racing, even as other racino operators worry that DFS could negatively affect racino revenue.[30] Some state-run lotteries are considering whether to offer online DFS games, while others are more concerned about losing customers to DFS.[31]

The American Gaming Association (AGA), which represents commercial and tribal casino operators, has taken the position that it seeks "legal clarity and adequate consumer protections" for DFS activities.[32] The Indian tribes that operate casinos generally have not weighed in on DFS, but some are concerned that it could affect gaming facilities that generated $28.5 billion in gross revenue in 2015.[33] In Arizona, the failure of a 2014 bill designed to legalize DFS was reportedly due in part to tribal objections.[34]

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[27] State of Nevada, Legislative Counsel Bureau, *Governor's Recommended Budget for the 2015-17 Biennium*, p. 15, March 2015, https://www.leg.state.nv.us/Division/Fiscal/Fiscal%20Report/2015/2015_FiscalReport.pdf.

[28] National Conference of State Legislatures (NCSL), "2015 Casino Taxes and Expenditures," September 28, 2015, http://www.ncsl.org/research/financial-services-and-commerce/casino-tax-and-expenditures-2013.aspx.

[29] Econsult Solutions, *The Current Condition and Future Viability of Casino Gaming in Pennsylvania*, May 2014, pp. 151-153, http://www.econsultsolutions.com/wp-content/uploads/PA-Gaming-Report-from-ESI_May-6.pdf.

[30] David Deitch, "Indiana Eyes Sports Betting, With Potentially Significant Implications for Daily Fantasy," *Legal Sports Report*, January 9, 2015.

[31] Currently, only Michigan, Illinois, and Georgia have online lotteries.

[32] J.D. Morris, "Vegas, Inc: Gaming Association Will Search for 'Rational Alternative' to Sports Betting Law," AGA, November 16, 2015, https://www.americangaming.org/vegas-inc-gaming-association-will-search-%E2%80%98rational-alternative%E2%80%99-sports-betting-law.

[33] Dustin Gouker, "Daily Fantasy Sports Industry Increasingly Running Into Tribal Gaming Concerns," *Legal Sports Report*, December 21, 2015, http://www.legalsportsreport.com/6950/dfs-and-tribal-gaming/; National Indian Gaming Commission (NIGC), "2014 Indian Gaming Revenues Increase 1.5%," press release, July 23, 2015, http://www.nigc.gov/news/detail/2014-indian-gaming-revenues-increase.

[34] Bob McManaman, "Future Clouded for Daily Fantasy Sports Betting," *Arizona Republic*, October 7, 2015, (continued...)

Legal Status and Regulatory Environment

Gambling is primarily a matter of state law, reinforced by federal law in situations where the presence of an interstate or foreign element might otherwise frustrate enforcement of state law. Few states have enacted laws that expressly address fantasy sports. However, state gambling laws often define "gambling" in such a way that they could potentially apply to fantasy sports, depending on the rules and format of the particular contest at issue. The legal status of fantasy sports under most state laws often turns on whether success in the activity depends primarily on the skill of individual contestants (which would likely make it legal) or mostly chance (which would probably make it unlawful gambling).[35] In addition, some state laws that would appear to permit "traditional" fantasy sports may not be as favorable toward DFS.

More than 80 civil lawsuits have been filed across the country against FanDuel and DraftKings; these cases allege improper or illegal conduct by the companies and advance three different theories of liability: (1) the use of "inside information" to gain an unfair advantage; (2) violations of state gambling laws; and (3) fraud relating to misleading promotional schemes.[36] In early February 2016, the U.S. Judicial Panel on Multidistrict Litigation consolidated these actions in a Massachusetts federal district court, noting that "these actions involve common questions of fact" and that "centralization … will serve the convenience of the parties and witnesses and promote the just and efficient conduct of this litigation."[37] Until these and other lawsuits involving DFS operators are settled, prosecutions become final, or states and the federal government definitively respond legislatively or administratively, questions will remain as to exactly what state and federal laws apply to these companies, their customers, and their service providers.

Federal Laws Potentially Applicable to DFS

DFS may implicate at least four federal laws that are directly related to gambling: (1) the Unlawful Internet Gambling Enforcement Act; (2) the Professional and Amateur Sports Protection Act; (3) the Wire Act; and (4) the Illegal Gambling Business Act. In addition, financial institutions that offer services to DFS operators could face legal liability under federal money laundering statutes if they do not implement adequate internal controls (policies and procedures) to manage and monitor risks.

Unlawful Internet Gambling Enforcement Act

The Unlawful Internet Gambling Enforcement Act (UIGEA) was enacted in 2006 as a response, in part, to the perceived problem of foreign Internet gambling operations that made their services available to U.S. customers.[38] The law attempts to address this issue by regulating the flow of

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http://www.azcentral.com/story/sports/nfl/cardinals/2015/10/03/future-clouded-daily-fantasy-sports-betting/73218872/.

[35] Marc Edelman, "A Short Treatise on Fantasy Sports and the Law: How America Regulates its New National Pastime," 3 *Harvard J. Sports & Entertainment Law* 1, pp. 26-29 (2012).

[36] U.S. Judicial Panel on Multidistrict Litigation, Case MDL No. 2678, Transfer Order Filed February 4, 2016, pp. 1-2, http://www.jpml.uscourts.gov/sites/jpml/files/MDL-2677_MDL-2678_MDL-2679-Initial_Transfer-01-16.pdf.

[37] Ibid., pp. 3-5. See also Bob McGovern, "Daily Fantasy Sports Suits Consolidated for Mass. Federal Court," *Boston Herald*, February 5, 2016.

[38] See, e.g., H.Rept. 109-412 (Pt.1), p. 8 (2006) ("[The Act's] primary purpose is to give U.S. law enforcement new, more effective tools for combating offshore Internet gambling sites that illegally extend their services to U.S. residents via the Internet"), and H.Rept. 109-412 (Pt. 2), p. 8 (2006) ("The booming industry of offshore websites accepting bets (continued...)

financial payments to companies that are involved in offering unlawful Internet gambling. Specifically, UIGEA prohibits anyone "engaged in the business of betting or wagering" from knowingly accepting checks, credit card charges, electronic transfers, and similar payments in connection with unlawful Internet gambling.[39] UIGEA expressly excludes from the definition of the term "business of betting or wagering" the services of financial institutions as well as communications and Internet service providers that may be used in connection with the unlawful bet;[40] however, such entities may nonetheless incur liability under UIGEA if they are directly engaged in the operation of an Internet gambling site.[41] A violation of UIGEA is subject to a criminal fine of up to $250,000 (or $500,000 if the defendant is an organization), imprisonment of up to five years, or both.[42] In addition, upon conviction the court may enter a permanent injunction enjoining a defendant from making bets or wagers "or sending, receiving, or inviting information assisting in the placing of bets or wagers."[43] Any person or entity that violates UIGEA and its implementing regulations may also be subject to civil and regulatory enforcement actions.[44]

UIGEA requires certain financial payment providers "to identify and block or otherwise prevent or prohibit restricted transactions"[45] that are used for unlawful Internet gambling. UIGEA does not, however, alter existing federal or state laws. Indeed, UIGEA contains a rule of construction provision that expressly pronounces its lack of preemption or other effect on other federal and state laws relating to gambling: "No provision of this subchapter shall be construed as altering, limiting, or extending any Federal or State law or Tribal-State compact prohibiting, permitting, or regulating gambling within the United States."[46]

In addition, UIGEA's definition of "unlawful Internet gambling" does not specify what gambling activity is illegal. As a federal appeals court emphasized in 2009, "[i]t bears repeating that the Act itself does not make any gambling activity illegal."[47] Rather, the statute relies on underlying federal or state gambling laws to make that determination—that is, UIGEA applies to an Internet bet or wager that is illegal in the place where it is placed, received, or transmitted:

> The term "unlawful Internet gambling" means to place, receive, or otherwise knowingly transmit a bet or wager by any means which involves the use, at least in part, of the Internet where such bet or wager is unlawful under any applicable Federal or State law in the State or Tribal lands in which the bet or wager is initiated, received, or otherwise made.[48]

UIGEA further defines the term "bet or wager" to mean "the staking or risking by any person of something of value upon the outcome of a contest of others, a sporting event, or a game subject to

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and wagers from persons located in the United States raises a number of social and criminal concerns related to Internet gambling").

[39] 31 U.S.C. §5363.

[40] 31 U.S.C. §5362(2).

[41] 31 U.S.C. §5367.

[42] 31 U.S.C. §5366(a).

[43] 31 U.S.C. §5366(b).

[44] 31 U.S.C. §§5364(e), 5365.

[45] 31 U.S.C. §5364(a).

[46] 31 U.S.C. §5361(b).

[47] *Interactive Media Entm't & Gaming Ass'n v. AG of the United States*, 580 F.3d 113, 117 (3d Cir. 2009).

[48] 31 U.S.C. §5362(10)(A).

chance, upon an agreement or understanding that the person or another person will receive something of value in the event of a certain outcome."[49] However, under UIGEA an illegal "bet" or "wager" specifically *does not include* "participation in any fantasy or simulation sports game … in which … no fantasy or simulation sports team is based on the current membership of an actual team that is a member of an amateur or professional sports organization" and that satisfies the following criteria:

1. All prizes and awards offered to winning participants are established and made known to the participants in advance of the game or contest, and their value is not determined by the number of participants or the amount of any fees paid by those participants.
2. All winning outcomes reflect the relative knowledge and skill of the participants and are determined predominately by accumulated statistical results of the performance of individuals (athletes, in the case of sports events) in multiple real-world sporting or other events.
3. No winning outcome is based (a) on the score, point spread, or any performance or performances of any single real-world team or a combination of such teams; or (b) solely on any single performance of an individual athlete in any single real-word sporting or other event.[50]

One argument underlying the fantasy sports exemption is that a player's command of statistics, knowledge of the game, and observation of factors affecting an individual athlete's performance are all matters of skill, not luck.

This fantasy sports exemption was enacted before the creation of DFS. In addition, the statutory exemption does not specify the extent to which chance may play a role in determining the winning outcome of the contest.[51] The UIGEA fantasy sports exemption also sets no limit on entry costs, prizes, or the duration of contests.[52] These three considerations form, in part, the basis for the legal uncertainty under which DFS providers may be able to assert their eligibility for the UIGEA exemption.

Professional and Amateur Sports Protection Act

The federal Professional and Amateur Sports Protection Act (PASPA),[53] enacted in 1992, generally prohibits state governments from sponsoring, operating, advertising, promoting, licensing, or authorizing gambling on competitive games in which amateur or professional athletes participate, "or on one or more performances of such athletes in such games."[54] It also prohibits any person from sponsoring, operating, advertising, or promoting such gambling "pursuant to the law or compact of a governmental entity."[55] (PASPA contained a "grandfather" clause to allow sports gambling operations in Nevada, Oregon, Delaware, and Montana, each of which permitted certain types of sports betting at the time of PASPA's passage.)[56]

[49] 31 U.S.C. §5362(1)(A).

[50] 31 U.S.C. §5362(1)(E)(ix).

[51] Zachary Zagger, "Outlook for Fantasy Sports Murky Amid Increased Scrutiny," *Law360.com*, September 18, 2015.

[52] I. Nelson Rose, "Are Daily Fantasy Sports Legal?," *Gaming Law Review and Economics*, June 2015.

[53] P.L. 102-559, codified at 28 U.S.C. §§3701 et seq.

[54] 28 U.S.C. §3702.

[55] 28 U.S.C. §3702(2).

[56] 28 U.S.C. §3704.

It is uncertain whether DFS or other types of fantasy sports leagues violate PASPA, particularly in light of the fantasy sports exemption that Congress included in UIGEA 14 years later. In addition, an argument has been made that PASPA may even preempt state laws that expressly legalize fantasy sports.[57] The Massachusetts Gaming Commission released a "white paper" on daily fantasy sports in January 2016 that explored in detail the possible "constraint to state action" toward DFS that PASPA may pose:

> The fact that PASPA prohibits a government entity "to sponsor, operate, advertise, promote, license or authorize *by law or compact*" suggests that conflict would only arise when a state passes legislation or joins a compact that involves one of the six PASPA verbs.… There is presently a dearth of case law discussing the limits of what would constitute affirmative state action sufficient to trigger a PASPA violation …
>
> Any approach to state action outside of the six PASPA verbs should be a cautious one … While some states have promulgated legislation to specifically exempt DFS from their definitions of gambling/bet/wager, such action could be challenged as "authorizing" or "promoting" a sports betting scheme particularly where a state would be required to take affirmative action to achieve the goal. Arguably, a state could defend its actions as merely clarifying the absence or ambiguity of existing law rather than an outright "authorization" that would run afoul of PASPA.
>
> Regulation that does not involve authorization by law is a significantly more conservative approach that appears far less likely to directly conflict with PASPA and has already been initiated by our attorney general. Further "regulate" is not one of the PASPA verbs and thus is arguably permitted on the face of the statute, particularly where the regulations themselves do not establish a licensing or other heavy state oversight scheme.
>
> Another method of avoiding the PASPA limitations may be to promulgate legislation that addresses the larger subject of internet-based electronic gambling. While DFS would likely fall under the umbrella of such legislation, if the legislation does not specifically target DFS, it runs less chance of any outright PASPA challenge.[58]

To date, no federal or state court has considered whether DFS operators, or state laws that regulate DFS, are in conflict with PASPA. However, PASPA provides that any legal challenge regarding this issue may be brought only by the U.S. Attorney General, the major professional sports leagues, or the National Collegiate Athletic Association (NCAA).[59] It is unclear whether any of these entities may be inclined to file a PASPA action. Several U.S. professional sports leagues have entered into partnerships with DFS operators, and thus might not desire to have a court determination of the impact of PASPA on DFS that is unfavorable to their economic interests.[60] On the other hand, the NCAA has long been an opponent of sports wagering involving its student athletes,[61] and has reportedly refused to allow DFS advertisements during college basketball tournaments; unless it changes its position, it could be a potential opponent of state actions legalizing DFS.[62] The U.S. Attorney General could also seek an injunction, but she may

[57] Daniel Wallach, "Fantasy Sports Legislation by States May Run Afoul of PASPA," *Sports Law Blog*, March 14, 2015, http://sports-law.blogspot.com/2015/03/fantasy-sports-legislation-by-states.html.

[58] Massachusetts Gaming Commission, *White Paper on Daily Fantasy Sports*, January 11, 2016, pp. 43-44 (emphasis in original), http://massgaming.com/wp-content/uploads/MGC-White-Paper-on-Daily-Fantasy-Sports-1-11-16.pdf.

[59] 28 U.S.C. §3703.

[60] Drew Harwell, "Move Over, Budweiser: Football Has a New Advertising King," *Washington Post*, September 16, 2015.

[61] "NCAA Position on Sports Wagering," http://www.ncaa.org/enforcement/sports-wagering.

[62] *See* Marc Tracy, "N.C.A.A. Distances Itself from Daily Fantasy Websites," *New York Times*, October 20, 2015 (reporting that "the N.C.A.A. had asked the [DFS] sites in August to stop offering fantasy games based on college (continued...)

be reluctant to do so, argues one legal practitioner, who cites "the deference that the federal government has historically provided to states related to the enforcement of gambling laws."[63]

Wire Act

The federal Wire Act[64] of 1961 (also referred to as the Interstate Wire Act or the Wire Wager Act) prohibits the use of interstate wire communication facilities by those in the gambling business to transmit bets or gambling-related information. Violators of the Wire Act are subject to imprisonment for not more than two years and/or a fine of the greater of not more than twice the gain or loss associated with the offense or $250,000 (not more than $500,000 for organizations).[65] Note that the Wire Act is directed at anyone "engaged in the business of betting or wagering," and some courts have suggested it may not be used to prosecute simple bettors.[66] Note also that the Wire Act applies without regard to whether the gambling is permitted under state law. The federal courts have interpreted the term "wire communications" to include Internet communications.[67]

Prior to 2011, the U.S. Department of Justice's Criminal Division consistently maintained that the Wire Act applies not only to sports wagering, but also to other forms of interstate gambling, including non-sports Internet gambling.[68] Such an expansive view of the Wire Act by the Justice Department apparently dissuaded state governments from expressly authorizing and implementing Internet gambling within their jurisdictions.[69] However, in late 2011, the Justice Department's Office of Legal Counsel reversed its interpretation of the Wire Act, opining that "interstate transmissions of wire communications that do not relate to a 'sporting event or contest,' 18 U.S.C. §1084(a), fall outside the reach of the Wire Act."[70] This decision expresses the Justice Department's intent to confine its use of the Wire Act to prosecutions of those involved in gambling businesses that use interstate wire communication facilities to transmit sports bets or sports gambling-related information.

(...continued)

sports 'because they were inconsistent with our values, bylaws, rules and interpretations regarding sports wagering' and could violate 'various state laws.'"); see also Marc Tracy, "ESPN and College Football Playoff Agree Not to Air Daily Fantasy Ads," *New York Times*, December 9, 2015.

[63] Andy Moore, "Does State Regulation of Fantasy Sports Violate PASPA?," *Law360.com*, December 8, 2015.

[64] 18 U.S.C. §1084.

[65] 18 U.S.C. §§1084(a), 3571(b),(d).

[66] *United States v. Scavo*, 593 F.2d 837, 843 (8th Cir. 1979) ("If an individual performs only an occasional or nonessential service or is a mere bettor or customer, he cannot properly be said to engage in the business"); but see *United States v. Southard*, 700 F.2d 1, 20 n.24 (1st Cir. 1983) ("The district court held that the statute did not prohibit the activities of 'mere bettors.' We take no position on this ruling except to point out that the legislative history is ambiguous on this point at best").

[67] *United States v. Lyons*, 740 F.3d 702, 716 (1st Cir. 2014) (discussing the Wire Act's "evident applicability to the internet"); *United States v. Cohen*, 260 F.3d 68, 76 (2d Cir. 2001) (holding that the transmission of bets over the Internet violated the Wire Act).

[68] For example, a Justice Department memorandum from 2010 noted that "[t]he Department has uniformly taken the position that the Wire Act is not limited to sports wagering and can be applied to other forms of interstate gambling." Memorandum for David Barron, Acting Assistant Attorney General, Office of Legal Counsel, from Lanny A. Breuer, Assistant Attorney General, Criminal Division (July 12, 2010), p. 3.

[69] Statement of Patrick Fleming, Poker Players Alliance, *Oversight Hearing on the U.S. Department of Justice Opinion on Internet Gaming: What's at Stake for Tribes: Hearing Before the Senate Comm. on Indian Affairs,* 112th Cong., 2d Sess., p. 2.

[70] Memorandum Opinion by Virginia A. Seitz, Assistant Attorney General, *Whether Proposals by Illinois and New York to Use the Internet and Out-of-State Transaction Processors to Sell Lottery Tickets to In-State Adults Violate the Wire Act*, September 20, 2011, http://www.justice.gov/olc/2011/state-lotteries-opinion.pdf.

It is unclear, however, whether operation of DFS or other types of fantasy or simulation sports games (as defined by the UIGEA exemption) constitutes "the placing of bets or wagers on any sporting event or contest" within the meaning of the Wire Act.

Illegal Gambling Business Act

DFS operators may face criminal liability under the Illegal Gambling Business Act of 1970 (IGBA)[71] if they are in violation of state gambling laws and meet other elements of the criminal offense. IGBA punishes anyone who conducts, finances, manages, supervises, directs, or owns all or part of an illegal gambling business. IGBA defines an "illegal gambling business" to mean a gambling business that

1. is a violation of the law of a state or political subdivision in which it is conducted;
2. involves five or more persons who conduct, finance, manage, supervise, direct, or own all or part of such business; and
3. has been or remains in substantially continuous operation for a period in excess of 30 days or has a gross revenue of $2,000 in any single day.

Violations of IGBA are punishable by imprisonment for not more than five years and/or fines of the greater of (1) not more than twice the gain or loss associated with the offense or (2) $250,000 ($500,000 for an organization).[72] Note that IGBA is broader than the Wire Act in one respect, as it applies to gambling activities that do not depend on the use of a "wire communication." However, IGBA is narrower than the Wire Act in that the type of illegal gambling business must first exceed the statutory thresholds described above in order for IGBA to apply. Reportedly, a federal grand jury in Florida has been investigating DFS companies for possible IGBA violations.[73]

Considerations for Financial Institutions Regarding DFS Transactions

The Bank Secrecy Act (BSA) of 1970[74] and its major component, the Currency and Foreign Transactions Reporting Act, require U.S. financial institutions to help the federal government detect and prevent money laundering[75] by filing reports and maintaining records of certain transactions involving cash, negotiable instruments, or foreign currency. Under the BSA, financial institutions[76] must file with the Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) suspicious activity reports (SARs) relating to any transaction involving $5,000 or more that they have reason to suspect are derived from illegal activity

[71] 18 U.S.C. §1955.

[72] 18 U.S.C. §§1955(a), 3571(d).

[73] William R. Levesque, "Attorney: Federal Grand Jury in Tampa Investigating Fantasy Sports Operators," *Tampa Bay Times*, October 10, 2015 (reporting that a "grand jury is looking into possible criminal violations involving the Illegal Gambling Business Act of 1970."); see also Alexandra Berzon & Sharon Terlep, "Fantasy Sports Trade Association Gets Subpoena From U.S. Prosecutor," *Wall Street Journal*, October 16, 2015 (noting that "[f]ederal law allows the U.S. government to prosecute companies that are violating state gambling laws," which is a likely reference to IGBA).

[74] 31 U.S.C. §§5311 et seq.

[75] For more information on the federal crime of money laundering, see CRS Report RL33315, *Money Laundering: An Overview of 18 U.S.C. 1956 and Related Federal Criminal Law*, by (name redacted)

[76] "Financial institutions" is defined very broadly under the BSA to include, among many other things, banks, insurance companies, travel agencies, casinos, and the U.S. Post Office. 31 U.S.C. §5312(a)(2).

(including illegal sports betting).[77] Banks must also establish and maintain anti-money laundering programs[78] designed to ensure that bank officers and employees will have sufficient knowledge of the banks' customers and of the business of those customers to identify the circumstances under which filing SARs is appropriate.[79] Suspicion aside, banks must file currency transaction reports with FinCEN relating to transactions involving $10,000 or more in cash.[80]

Banks, their officers, employees, and customers may also face criminal liability under the money laundering statutes for illegal gambling-related financial transactions. Section 1957 of Title 18, *U.S. Code*, makes it a federal crime to deposit or withdraw $10,000 or more in proceeds derived from illegal gambling activities.[81] Section 1956 makes it a federal crime to engage in a financial transaction involving such proceeds conducted with an eye to promoting further offenses—for example, by withdrawing illegal gambling-generated funds in order to pay the salaries of the gambling operator's employees.[82]

Federally insured state- and federally chartered depository institutions that engage in illegal or unsafe banking practices also run the risk of being assessed civil money penalties and even losing deposit insurance coverage, which would result in the termination of their status as insured depository institutions.[83]

Finally, banks, credit card companies, and other payment system participants could be at risk of violating UIGEA if they process transactions for DFS companies that are operating in states where DFS has been deemed unlawful. In apparent concern about its legal liability under UIGEA due to the growing number of state attorneys general who have determined DFS to be illegal gambling (see detailed description of these actions in the following section), a payment processing company, Vantiv Entertainment Solutions, informed its DFS clients that it would "suspend all processing for payment transactions" related to DFS in the United States effective February 29, 2016. Because this company "handles a significant number of transactions" for FanDuel and DraftKings in the form of players' deposits and withdrawals, one report called its decision to stop working with them "perhaps the biggest blow yet" to the DFS industry.[84] A week after Vantiv's action, the world's largest credit card lender, Citigroup, announced that it would "block transactions at DraftKings and FanDuel by New York residents pending a final decision by the courts."[85] These combined actions arguably "threaten the financial lifeblood of the [DFS] industry" because "Citigroup provides money through its cards, while the other financial institution, Vantiv, processes the bets."[86]

[77] 21 U.S.C. §5318(g); 31 C.F.R. §1020.320.
[78] 31 U.S.C. §5318(h); 12 U.S.C. §1818(s); 12 U.S.C. §1786(q)(1).
[79] 31 C.F.R. §§1020.200-1020.220.
[80] 31 U.S.C. §5313; 31 C.F.R. subpt.1020C; 31 C.F.R. subpt.1010 C.
[81] 18 U.S.C. §§1957(a), (d).
[82] 18 U.S.C. §1956(a)(1)(A)(i).
[83] 12 U.S.C. §1818.
[84] Joe Drape, "Payment Processor to Stop Working with Daily Fantasy Sports Clients," *New York Times*, January 29, 2016, http://www.nytimes.com/2016/01/30/sports/draftkings-fanduel-vantiv-daily-fantasy.html.
[85] Zachary Zagger, "Citigroup Halts DraftKings, FanDuel Transactions in NY," *Law360.com*, February 5, 2016 (quoting a Citigroup spokeswoman).
[86] Walt Bogdanich et al., "Fantasy Sites Are Dealt New Rebuff by Citigroup," *New York Times*, February 5, 2016.

State Action

Any entity that provides gaming for real money must comply with state gambling laws to be offered in a state. Each state has its own independent definition of gambling, which may include everything from state-conducted lotteries, bricks-and-mortar casinos, horse racing, and tribal casinos to intrastate Internet gambling. The issue of whether DFS is considered a game of luck or skill is central to the debate over the legal status of DFS under the states' gambling laws.

State Legislatures

The number of states taking a legislative interest in DFS is growing rapidly. In 2015, DFS was an active topic for lawmakers in least a dozen states, up from just two in 2014.[87] Some states are considering requiring DFS operators to obtain licenses and comply with certain consumer protection safeguards (such as employee background checks and ensuring that players are not underage or employed by a DFS company); others are interested in regulating the industry as they regulate gambling; still others are seeking to clarify its status under their existing gambling laws.[88] For example, Maryland in 2012 enacted a law explicitly legalizing fantasy sports contests by exempting "fantasy competition" from state law prohibitions against betting, wagering, and gambling.[89] In 2015, Kansas also enacted a law declaring fantasy sports a game of skill—thus removing fantasy sports from state laws that ban illegal lotteries.[90] In October 2015, Nevada became the first state to require gambling licenses for DFS operators, via a notice issued by the Nevada Gaming Control Board.[91]

Some DFS operators do not offer fantasy sports competitions in states where their legal status is unclear. For example, FanDuel and DraftKings do not offer DFS games in Arizona, Hawaii, Iowa, Louisiana, Mississippi, Montana, Nevada, and Washington.[92] Arizona law limits fantasy sports contests by defining prohibited gambling as an "act of risking or giving something of value for the opportunity to obtain a benefit from a game or contest of chance or skill or a future contingent event."[93] An Iowa criminal statute prohibits the playing of a "game for any sum of money or other property of any value,"[94] which was interpreted by a 1931 Iowa Supreme Court decision as not depending on "whether the game is one of skill or chance."[95] Louisiana passed a law in 1997 that established the crime of "gambling by computer," which prohibits the operation of "any game or contest whereby a person risks the loss of anything of value in order to realize a profit when

[87] Gambling Compliance, *U.S. Internet Gambling Regulatory Tracker*, November 2015, p. 19.

[88] For a list of state legislative activity regarding DFS, see Legal Sports Report, "Legislative Tracker: Daily Fantasy Sports, Sports Betting," at http://www.legalsportsreport.com/dfs-bill-tracker/.

[89] Maryland Criminal Law Code Ann. §12-114; Greg Masters, "Fantasy Football Joins Md. Legislature's Late-Session Frenzy," *Washington Post*, March 16, 2012.

[90] Kansas enacted HB 2155, which legalized real-money fantasy sports in the state by exempting fantasy contests from the state's legal code, effective July 1, 2015. See also Nicholas Clayton, "Bill Legalizing Fantasy Sports Clears Kansas Legislature," *Associated Press*, May 7, 2015.

[91] A.G. Burnett, Chairman, Nevada Gaming Control Board, *Legality of Offering Daily Fantasy Sports in Nevada*, October 15, 2015, http://gaming.nv.gov/modules/showdocument.aspx?documentid=10481.

[92] See DraftKings "Terms of Use" at https://www.draftkings.com/help/terms; FanDuel "Terms of Use" at https://www.fanduel.com/terms (last visited February 22, 2016).

[93] Arizona Ann. Revised Stat. §13-3301. See also Ariz. Att'y Gen. Op. No. I98-002, 1998 WL48550, issued January 21, 1998, which concludes that "[s]ports pools, fantasy football, and card and dice games involving a wager are gambling under Arizona law."

[94] Iowa Code §725.7(1)(a).

[95] *Parker-Gordon Importing Co. v. Benakis*, 238 N.W. 611, 613 (Iowa 1931).

accessing the Internet."[96] Montana law expressly prohibits any form of commercial gambling, which would include fantasy sports in which entrance fees are paid and prizes are awarded.[97] The Washington State Constitution prohibits all forms of gambling unless the activity is specifically allowed by state law,[98] and Washington law also expressly prohibits Internet gambling.[99] The Washington State Gambling Commission has stated that fantasy sports wagering falls under both the statutory definition of gambling as well as the state statute prohibiting Internet gambling (to the extent the particular fantasy sports wagering takes place online).[100] Finally, as described in greater detail in the next section, FanDuel and DraftKings have suspended their operations in Hawaii, Mississippi, and Nevada in the aftermath of opinions issued by those states' attorneys general that called into question the legality of DFS.

Illinois is considering a bill that has garnered support from DFS operators, who see it as an industry-friendly measure that could be used as a model for regulation in other states. Included in Illinois's Fantasy Contests Act are provisions that would define fantasy sports without equating it to gambling, ban players under age 18, and require annual audits to make certain that state rules are being followed.[101]

In late January 2016, the California Assembly overwhelmingly approved a bill, the Internet Fantasy Sports Games Consumer Protection Act, which would establish a regulatory and licensing regime for DFS operators.[102] If enacted, the bill would require any person or entity to obtain a license from the California Department of Justice prior to offering any Internet fantasy sports within the state. The licensed operator would be required to pay an annual regulatory fee and also provide player-winnings information to California tax authorities.[103]

Five states account for roughly 40% of all DFS usage (see **Figure 2**) and about 40% of industry revenues.[104] This suggests that if these states pass legislation that negatively affects DFS businesses, the growth of the industry could be adversely affected.

[96] Louisiana Revised Stat. §14:90.3.

[97] Montana Code Ann. §23-5-802 ("It is unlawful to wager on a fantasy sports league by telephone or by the internet.").

[98] Wash. Const. Art. II, §24.

[99] Rev. Code of Washington §9.46.240.

[100] Washington State Gambling Commission, *Online Gambling*, http://www.wsgc.wa.gov/publications/brochures/5-165-internet-gambling-brochure.pdf.

[101] H.B. 4323, Fantasy Contests Act, http://www.ilga.gov/legislation/billstatus.asp?DocNum=4323&GAID=13&GA=99&DocTypeID=HB&LegID=92715&SessionID=88.

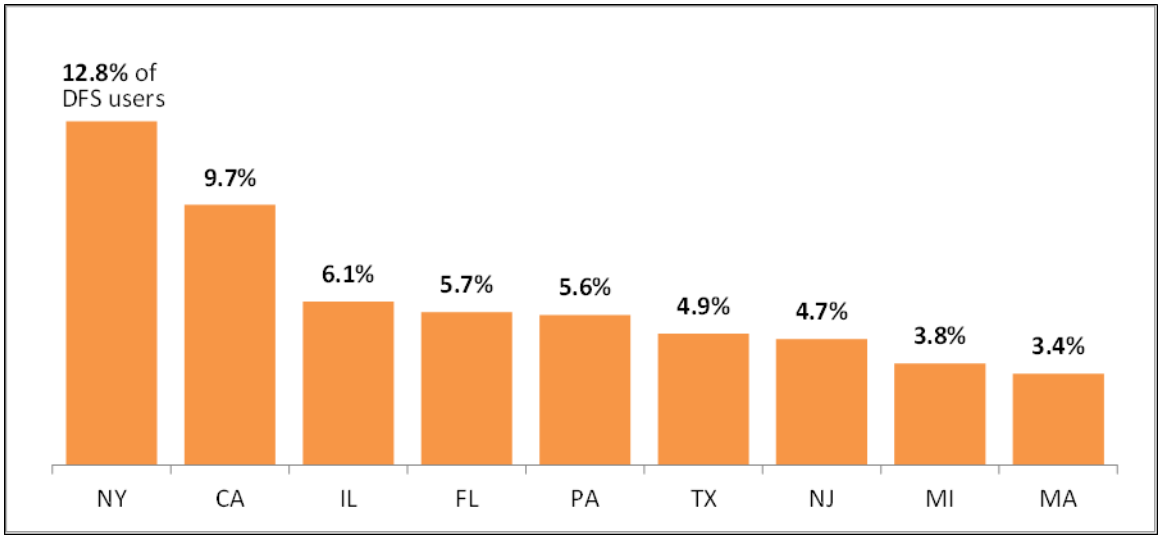
[102] Patrick McGreevy, "Bill Legalizing Fantasy Sports Websites in California Makes it Out of State Assembly," *Los Angeles Times*, January 27, 2016.

[103] A.B. 1437, Internet Fantasy Sports Game Protection Act, available at https://leginfo.legislature.ca.gov/faces/billTextClient.xhtml?bill_id=201520160AB1437.

[104] Adam Krejcik and Chris Grove, *Daily Fantasy Sports Industry Update*, Eilers Research, November 2015, p. 6.

Figure 2. DFS Usage by State

Estimated, November 2015



Source: Eilers Research, "*Daily Fantasy Sports Industry Update*," p. 6, November 2015.

State Attorneys General

Parallel to the DFS activity in state legislatures, several state attorneys general have weighed in on the legal status of daily fantasy sports under their existing laws. To date, the majority have determined DFS to constitute illegal gambling, although a few have approved of the contests. For example, Nevada's attorney general in October 2015 found that "daily fantasy sports constitute sports pools and gambling games.… As a result, pay-to-play daily fantasy sports cannot be offered in Nevada without licensure."[105] In November 2015, the New York attorney general ruled that DFS is illegal gambling and ordered the two largest DFS websites to immediately stop accepting wagers in the state.[106] In his cease-and-desist letter to FanDuel, he distinguished season-long fantasy sports from DFS:

> We believe there is a critical distinction between DFS and traditional fantasy sports, which, since their rise to popularity in the 1980s, have been enjoyed and legally played by millions of New York residents. Typically, participants in traditional fantasy sports conduct a competitive draft, compete over the course of a long season, and repeatedly adjust their teams. They play for bragging rights or side wagers, and the Internet sites that host traditional fantasy sports receive most of their revenue from administrative fees and advertising, rather than profiting principally from gambling. For those reasons among others, the legality of traditional fantasy sports has never been seriously questioned in New York.
>
> Unlike traditional fantasy sports, the sites hosting DFS are in active and full control of the wagering: FanDuel and similar sites set the prizes, control relevant variables (such as

[105] Office of the Nevada Attorney General, Gaming Division, *Memorandum Regarding the Legality of Daily Fantasy Sports Under Nevada Law*, October 16, 2015, p. 2, http://www.legalsportsreport.com/wp-content/uploads/2015/10/Nevada-AG-DFS.pdf.

[106] New York State Office of the Attorney General, "A.G. Schneiderman Issues Cease-And-Desist Letters to FanDuel And DraftKings, Demanding That Companies Stop Accepting Illegal Wagers in New York State," November 11, 2015, http://www.ag.ny.gov/press-release/ag-schneiderman-issues-cease-and-desist-letters-fanduel-and-draftkings-demanding.

> athlete "salaries"), and profit directly from the wagering. FanDuel has clear knowledge and ongoing active supervision of the DFS wagering it offers. Moreover, unlike traditional fantasy sports, DFS is designed for instant gratification, stressing easy game play and no long-term strategy. For these and other reasons, DFS functions in significantly different ways from sites that host traditional fantasy sports.[107]

On December 11, 2015, a New York State court judge granted the New York attorney general's request for preliminary injunctions against DraftKings and FanDuel (to stop them from doing business in New York and accepting bets entry fees, wagers, or bets from New York consumers).[108] Later that same day, the DFS companies obtained a temporary stay of the preliminary injunctions from a New York appellate court.[109] In early January 2016, the New York Supreme Court Appellate Division's First Department granted the DFS companies' requests for permanent stays of the injunctions pending their appeal of the judge's order.[110] According to one news report, the appeal has been scheduled for May 2016.[111]

Although Maryland enacted a law in 2012 that permits fantasy sports, the Maryland attorney general in January 2016 issued an advisory opinion questioning whether DFS is authorized by that law and recommended that the Maryland state legislature consider the issue.[112] Attorneys general in other states have also determined that DFS constitutes illegal gambling under their state laws, including in Illinois,[113] Texas,[114] Vermont,[115] Hawaii,[116] and Mississippi.[117]

Reaching an opposite conclusion, the Massachusetts attorney general announced in October 2015 that she believes DFS is not prohibited by either federal or Massachusetts state law.[118] She later

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[107] New York State Office of the Attorney General, *Notice to Cease and Desist and Notice of Proposed Litigation Pursuant to New York Executive Law § 63(12) and General Business Law § 349*, November 10, 2015, p. 2, http://ag.ny.gov/pdfs/Final_NYAG_FanDuel_Letter_11_10_2015_signed.pdf.

[108] Brent Schrotenboer et al., "New York Judge Orders Shutdown of DraftKings, FanDuel," *USA Today*, December 11, 2015.

[109] Sharon Terlep, "Appeals Court Lets DraftKings, FanDuel Continue in New York," *Wall Street Journal*, December 11, 2015.

[110] Joe Drape, "Court Allows FanDuel and DraftKings to Operate in New York Amid Appeal," *New York Times*, January 11, 2016.

[111] Darren Rovell and David Purdum, "New Yorkers Can Play Daily Fantasy While Case Makes Way Through Court," ESPN.com, January 11, 2016, http://espn.go.com/chalk/story/_/id/14549053/draftkings-fanduel-remain-open-new-york-players-appeal.

[112] Attorney General of Maryland Letter to the Honorable Thomas V. Mike Miller, Jr., January 15, 2016, http://www.legalsportsreport.com/wp-content/uploads/2016/01/Miller-01-15-16.pdf, p. 22 ("[B]ecause the legislative history … suggests that the General Assembly did not focus on the regulation of daily fantasy sports in 2012, and could not realistically have considered daily fantasy sports as they exist today, we recommend that the Legislature squarely take up the issue this session and clarify whether daily fantasy sports are authorized in Maryland").; See also Jeff Barker, "Daily Fantasy Sports Games May Not Be Legal in Maryland, Attorney General Says," *Baltimore Sun*, January 15, 2016.

[113] Office of Attorney General Lisa Madigan, State of Illinois, File No. 15-006, December 23, 2015, http://www.illinoisattorneygeneral.gov/opinions/2015/15-006.pdf; see also Carlos Sadovi, "Attorney General: Daily Sports Fantasy Betting Illegal Under Illinois Law," *Chicago Tribune*, December 23, 2015.

[114] Attorney General of Texas Ken Paxton, *The Legality of Fantasy Sports Leagues Under Texas Law*, Opinion No. KP-0057, January 19, 2016, https://texasattorneygeneral.gov/opinions/opinions/51paxton/op/2015/kp0057.pdf.

[115] Scott Malone, "Fantasy Sports Illegal in Vermont, Attorney General's Office Says," *Reuters*, January 15, 2016.

[116] Curt Woodward, "Hawaii AG Says Fantasy Sports Illegal, No Enforcement Yet," *Boston Globe*, January 28, 2016.

[117] Mary Perez, "Jim Hoods: Fantasy Sports Betting Illegal in Mississippi," *Sun Herald*, January 29, 2016, http://www.sunherald.com/news/business/casino-gambling/article57335733.html.

[118] Steve Annear, "Maura Healey Says DraftKings Operation is Legal," *Boston Globe*, October 7, 2015.

issued the proposal mentioned above, laying out extensive regulations under which she would like to see DFS companies operate, including a ban on players under 21 and restrictions on where such sites can advertise.[119] In early February 2016, Rhode Island's attorney general found that DFS leagues do not violate state laws pertaining to "games of chance" and lotteries; nevertheless, he recommended that the Rhode Island legislature act expeditiously to enact a statute that regulates the operation of DFS "to ensure criminal elements do not infiltrate the game, youth participation is barred, [and] addiction issues [are] addressed."[120]

DFS-Related Consumer Protection Concerns

The popularity of DFS and its unregulated status have generated a number of concerns related to protection of consumers who enter daily fantasy sports contests.

Player Funds

It is not clear what legal protections DFS customers have over their account balances upon the default or insolvency of a DFS company. DFS companies currently are not subject to comprehensive regulatory regimes at the federal level or in most states.[121] Instead, many DFS companies are FSTA members, through which they *voluntarily* agree to comply with industry standards.[122]

One FSTA standard calls for companies to segregate customer deposits from their general operating funds.[123] FanDuel and DraftKings have stated publicly that they adhere to the policy of ring-fencing customer deposits in segregated customer accounts.[124] However, it is unclear whether the consumer protections outlined in these public statements and voluntary industry standards are legally binding and enforceable.

Each DFS company requires individuals to agree to a "terms of service agreement" before they can enter contests.[125] These terms of service agreements contractually establish the general legal relationship between the DFS company and its customers. At least some terms of service agreements, which vary from company to company, arguably are ambiguous as to a customer's legal recourse when the company fails, for example, by entering bankruptcy. These agreements might, for instance,[126]

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[119] Attorney General of Massachusetts, *AG Healey Proposes Strong Consumer Protection Regulations for Daily Fantasy Sports Operations in Massachusetts*, November 19, 2015, http://www.mass.gov/ago/news-and-updates/press-releases/2015/2015-11-19-daily-fantasy-sports.html.

[120] Rhode Island Attorney General Peter F. Kilmartin's Opinion Regarding Daily Fantasy Sports, February 4, 2016, p. 3, http://www.legalsportsreport.com/wp-content/uploads/2016/02/Rhode-Island-DFS-Opinion.pdf; see also Paul Edward Parker, "AG Says Daily Fantasy Sports Websites like FanDuel, DraftKings Legal in R.I.," *Providence Journal*, February 4, 2016.

[121] See the discussion in this report on "Legal Status and Regulatory Environment."

[122] See FSTA, Paid Entry Contest Operator Charter, *available at* http://fsta.org/about/fsta-paid-entry-contest-operator-charter/.

[123] Ibid.

[124] See, e.g., Chris Grove, "A Call For All Daily Fantasy Sports Operators To Increase Transparency Regarding Player Funds," *Legal Sports Report*, October 15, 2015, http://www.legalsportsreport.com/5105/dfs-player-funds/.

[125] See, e.g., "FanDuel Terms of Use," last updated November 17, 2015, https://www.fanduel.com/terms; DraftKings "Terms of Use," last updated February 3, 2016, https://www.draftkings.com/help/terms.

[126] See, generally, ibid., and Chris Grove, "A Call For All Daily Fantasy Sports Operators To Increase Transparency Regarding Player Funds," *Legal Sports Report*, October 15, 2015, http://www.legalsportsreport.com/5105/dfs-player-(continued...)

- inadequately or imprecisely define what constitutes "customer funds" or "customer deposits";
- fail to require that customer deposits be held at financial institutions that are insured by federal or state governments;
- fail to require that customer accounts be held and administered by independent third parties;
- expressly state that the agreement does not create a fiduciary or similar legal relationship between the customer and the DFS company;
- allow the DFS company to unilaterally amend the terms of agreement at any time and for any reason;
- allow the DFS company to deny prizes or "points" for amorphous reasons, such as if a customer has engaged in an activity that the company considers to be "adverse to [its] operation";[127]
- fail to establish what rights a customer might have to recover funds if the customer's account is canceled by the DFS operator for a violation of the terms of service agreement; and
- include liability waiver provisions.[128]

Additionally, players may have difficulty verifying that companies are complying with industry standards and stated policies to the extent that DFS companies are not subject to comprehensive regulatory regimes. Furthermore, even if customer funds are fully protected, there may be a significant delay in customers' ability to recover their funds if a DFS company enters a bankruptcy or some other legal proceeding.[129]

Age Limits

States typically set a minimum age for persons engaging in casino gambling and racetrack betting, but age limits are more difficult to enforce for games offered online. Massachusetts has proposed prohibiting anyone under age 21 from participating in daily fantasy sports games.[130] Some DFS operators request potential players to supply copies of identification documents if there is reason to suspect a minor is creating an account, and DraftKings requires new players to state their dates of birth.

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funds/.

[127] "FanDuel Terms of Use," last updated November 17, 2015, https://www.fanduel.com/terms.

[128] FanDuel's current terms of service agreement requires customers to acknowledge that "your use of the site and service is at your own risk. recognizing such, you understand and agree that, to the fullest extent permitted by applicable law, neither FanDuel nor its suppliers or licensors will be liable to you for any direct, indirect, incidental, special, consequential, punitive, exemplary or other damages of any kind, including without limitation damages for loss of profits, goodwill, use, data or other tangible or intangible losses or any other damages based on contract, tort, strict liability or any other theory (even if FanDuel had been advised of the possibility of such damages).... " "FanDuel Terms of Use," last updated November 17, 2015, https://www.fanduel.com/terms.

[129] Will Hobson, "DraftKings, FanDuel FBI Investigation Could Freeze Daily Fantasy Players' Money for Years," *Washington Post*, October 20, 2015, https://www.washingtonpost.com/news/sports/wp/2015/10/20/draftkings-fanduel-fbi-investigation-could-freeze-daily-fantasy-players-money-for-years/.

[130] Office of the Attorney General of Massachusetts, "Daily Fantasy Sports, Draft Regulations 940 C.M.R. 34.00," November 19, 2015, http://www.legalsportsreport.com/6385/massachusetts-ag-dfs-regulation/.

Inside Information

In fall 2015, it was reported that employees of FanDuel and DraftKings had won large prizes playing at other DFS sites, possibly by using nonpublic information as to how many people selected specific National Football League players for their teams.[131] Two Members of Congress called upon the Federal Trade Commission (FTC) to investigate whether these incidents involving possible misuse of private information constitute an "unfair or deceptive practice" under the Federal Trade Commission Act.[132] In response to these allegations, FanDuel and DraftKings prohibited their employees from playing DFS games on any DFS website.[133] The Massachusetts attorney general has also proposed regulations that would forbid any DFS employee or contractor from playing on any DFS contest platform, "[n]or may such person play through another person as a proxy."[134]

Problem Gambling

Because players may participate in DFS from homes, offices, dormitory rooms, or any number of other locations at any time of day or night, some individuals may find their desire to play difficult to control.[135] The National Council on Problem Gambling (NCPG) adopted a resolution on October 8, 2015, stating it believes participants in fantasy sports are at high risk to, and do, develop gambling problems. Among other things, it urges companies offering fantasy sports contests to develop gambling-related consumer protections using NCPG guidelines as a foundation,[136] and to avoid running advertisements that "misrepresent the frequency or extent of winning or target people with game-play problems or minors ..."[137] The Massachusetts attorney general's proposed DFS regulations would require DFS operators to comply with the state's "truthful advertising" regulations and to not use in any advertisements the depictions of minors, students, or school or college settings.[138] Furthermore, the proposed regulations mandate that "advertisements in published media (e.g., print, television, Internet and smartphone applications) will include information concerning assistance available to problem gamblers or will direct consumers to a reputable source for such information."[139]

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[131] Joe Drape & Jacqueline Williams, "In Fantasy Sports, Signs of Insiders' Edge," *New York Times*, October 11, 2015; Des Bieler, "Insider-Trading Scandal Rocks Daily Fantasy Sports Industry," *Washington Post*, October 5, 2015.

[132] Letter from Senator Robert Menendez and Representative Frank Pallone to Edith Ramirez, Chairwoman, FTC, October 6, 2015, http://www.menendez.senate.gov/imo/media/doc/Daily%20Fantasy%20Sports%20Games.pdf.

[133] Sarah E. Needleman & Sharon Terlep, "FanDuel, DraftKings Ban Employees From Playing Daily Fantasy Contests for Money," *Wall Street Journal*, October 7, 2015; FanDuel, "Statement to Our Users," October 7, 2015, https://newsroom.fanduel.com/2015/10/07/statement-to-the-press/ ("We have permanently banned our employees from playing any daily fantasy games for money, on any site. We will also require all customers to confirm that they are not an employee of any other third party fantasy site, and if they are, they will not be allowed to access our site.").

[134] Draft Regulations 940 C.M.R. 34.12(1).

[135] Stop Predatory Gambling, "*Use Promo Code INEQUALITY*, Inside Online Fantasy Sports Gambling and the Misleading, Unfounded Lobbying Push for 'Government Regulation,'" November 2015, p. 15, http://stoppredatorygambling.org/wp-content/uploads/2015/11/2015-Report-on-Online-Fantasy-Sports-Gambling.pdf.

[136] National Council on Problem Gambling (NCPG), "Resolution of the NCPG Board of Directors Regarding Fantasy Sports," press release, October 8, 2015, http://www.ncpgambling.org/wp-content/uploads/2015/10/NCPG-Fantasy-Sports-Resolution-Oct-2015.pdf.

[137] NCPG, "Fantasy Sports Consumer Protection Guidelines," December 4, 2015, p. 4, http://www.ncpgambling.org/wp-content/uploads/2014/04/Fantasy-Sports-Consumer-Protection-Guidelines-Final-December-4-2015.pdf.

[138] Draft Regulations 940 C.M.R. 34.07(1), (2).

[139] *Id.* 940 C.M.R. 34.07(4).

Proof of Location

If state governments regulate DFS, operators will need to be able to ensure players are where they say they are. The same is true if DFS is found to be gambling, as UIGEA specifically prohibits "gambling businesses from knowingly accepting payments in connection with the participation of another person in a bet or wager that involves the use of the Internet and that is unlawful under any federal or state law."[140]

Some gambling businesses, such as poker websites, currently use geolocation technology to assure that players are physically located in jurisdictions in which the games are legal. The same technology could probably be applied to DFS. DraftKings recently announced an agreement with GeoComply, a company that tracks user location by analyzing Internet protocol (IP) addresses and Global Positioning System data, triangulating wi-fi and cell tower connections, and employing software to detect a customer's use of concealing technologies such as virtual private networks. FanDuel has declined to say what geolocation technology and procedures it uses.[141]

Congressional Efforts and Policy Considerations

No bills have been introduced in the 114th Congress that would either legalize or regulate DFS nationwide. However, some Members have called for formal inquiries into the daily fantasy sports industry.[142]

In October 2015, Representative Hakeem Jeffries asked the House Judiciary Committee to examine whether "permitting a multibillion-dollar industry to police itself serves the best interests of the American people."[143] Senator Robert Menendez and Representative Frank Pallone have called on the Federal Trade Commission (FTC) to implement safeguards and ensure a fair playing field in daily fantasy sports.[144] And Senator Richard Blumenthal has called for a federal investigation into deceptive or fraudulent practices at DFS leagues by the FTC and the Department of Justice.[145] In addition, questions about the roles of skill and luck in fantasy sports prompted Representative Frank Pallone in September 2015 to request the House Energy and Commerce Committee to hold a hearing to consider whether fantasy sports is currently allowed by UIGEA.[146] According to press reports, Representative Dina Titus, too, has asked the House Energy and Commerce Committee to hold a hearing on the legalities of daily fantasy sports.[147]

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[140] Federal Deposit Insurance Corporation (FDIC), *Unlawful Internet Gambling Enforcement Act Examination Guidance and Procedures*, Unlawful Internet Gambling Enforcement Act of 2006, Overview, FIL-35-2010, June 30, 2010, p. 1, https://www.fdic.gov/news/news/financial/2010/fil10035a.pdf.

[141] Steve Ruddock, "What Kind of Geolocation Methods Are Daily Fantasy Sports Sites Using, and How Effective Are They?," *Online Poker Report*, October 19, 2015, http://www.onlinepokerreport.com/18535/dfs-gelocation-questions/.

[142] Todd Ruger, "As Super Bowl 50 Approaches, Spotlight Shines on Fantasy Sports Sites," *CQ Weekly*, February 1, 2016, pp. 1-2, 5.

[143] Office of Congressman Hakeem Jeffries, "Rep. Jeffries Calls for House Judiciary Committee Hearing on the Online Fantasy Sports Industry," press release, October 6, 2015, https://jeffries.house.gov/media-center/press-releases/rep-jeffries-calls-for-house-judiciary-committee-hearing-into-online.

[144] Office of Congressman Frank Pallone, "Pallone, Menendez Call for Fairness in Daily Fantasy Sports, Outside MetLife Stadium," press release, October 13, 2015, https://pallone.house.gov/press-release/pallone-menendez-call-fairness-daily-fantasy-sports-outside-metlife-stadium.

[145] Office of U.S. Senator Richard Blumenthal, "Blumenthal Calls on DOJ, FTC to Investigate Deception and Fraud in Daily Fantasy Sports Betting," press release, October 12, 2015, http://www.blumenthal.senate.gov/newsroom/press/release/blumenthal-calls-on-doj-ftc-to-investigate-deception-and-fraud-in-daily-fantasy-sports-betting.

[146] Letter from Representative Frank Pallone to Representative Fred Upton, Chairman, Committee on Energy and (continued...)

Policy options that could shape the future of the DFS industry generally center on whether regulation should come from Congress, individual states, or the DFS industry itself.

Federal Regulation

Congress could pass legislation specifically governing DFS games, such as laws to oversee state and tribal agencies that regulate DFS contests. Congress could also amend the existing federal gambling laws to expressly prohibit or authorize DFS gaming. Arguably, if Congress imposes regulations on DFS providers, it would likely affect the industry's costs, as new laws may include new costs such as significant consumer protections and licensing fees.

State Regulation

Currently, a state-by-state approach is being used to regulate the industry. For example, Nevada now requires a DFS operator to obtain a license. Some states, such as Massachusetts, may regulate the DFS industry within their borders, and others, like Texas, may declare it unlawful gambling. A few states, specifically Kansas, may allow DFS companies to continue as an unregulated industry. Some states, for instance New York, might attempt to halt DFS operators until regulations are put in place. Litigation over some of these state actions is currently ongoing, and additional lawsuits are possible in the future.

Industry Self-Regulation

The DFS industry has responded to greater national and state scrutiny with its own self-regulatory system. In October 2015, FSTA, which claims more than 300 member companies, including DraftKings, FanDuel, Yahoo Fantasy Sports, ESPN, and CBS Sports Digital, announced a Fantasy Sports Control Agency (FSCA).[148] FSCA, led by Seth Harris, former acting U.S. Secretary of Labor, aims to develop cross-company standards, internal controls, auditing policies, and enforcement mechanisms to govern the industry. Both DraftKings and FanDuel have endorsed FSCA's formation.

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Commerce, September 14, 2015, https://democrats-energycommerce.house.gov/sites/democrats.energycommerce.house.gov/files/hearing%20request%20Fantasy%20Sport%20Sept14.2015.pdf.

[147] Howard Stutz, "Titus Wants Congress to Look into Legalities of Daily Fantasy Sports," *Las Vegas Review-Journal*, October 8, 2015, http://www.reviewjournal.com/politics/titus-wants-congress-look-legalities-daily-fantasy-sports.

[148] FSTA, "Fantasy Sports Trade Association Appoints Acting U.S. Secretary of Labor Seth D. Harris to Spearhead Fantasy Sports Control Agency," press release, October 27, 2015, http://fsta.org/fantasy-sports-trade-association-appoints-former-acting-u-s-secretary-of-labor-seth-d-harris-to-spearhead-fantasy-sports-control-agency/.

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