Tackling Daily Fantasy Sports in the States

BY JAKE LESTOCK

What began as a season-long activity for friends acting as sports team owners to win cash prizes and bragging rights has now evolved into a multi-billion-dollar business. Fantasy sports contests are a type of game in which participants assemble imaginary teams made up of real athletes. These teams compete against each other based on how well their players perform in actual matches. Winning team “owners” earn cash prizes. The Fantasy Sports Trade Association (FSTA) estimates that in 2017, 59.3 million people played fantasy sports in the U.S. and Canada and spent an average of $556 a year on related costs.

While these types of contests have been going on since the 1980s, the games have evolved into a new industry known as daily fantasy sports (DFS), which has spread throughout the country in the past few years, fostering the growth of new billion-dollar companies.

Much like traditional fantasy sports, daily fantasy sports are games in which players compete against others by paying an entry fee to build a team of athletes from a sports league. Players earn points based on the statistical performance of the participants in real-world competitions. The main difference is that DFS games are played in a single day or week, as opposed to an entire season, which gives players a chance to win—or lose—money more frequently.

Federal Action

The legality of fantasy sports has been a constant topic of discussion in the DFS debate. The most common argument is whether daily fantasy sports constitute “games of skill” or “games of chance.” The Unlawful Internet Gaming Enforcement Act (UIGEA) of 2006, which prevents financial institutions in the U.S. from processing transactions related to online gambling, classified fantasy contests as games of skill, thus exempting them from the law. However, the act’s language is vague enough to place the games in a legal grey area for Congress and the states to determine individually.

Thus far, Congress has had little involvement in this debate. The U.S. House Subcommittee on Commerce, Manufacturing and Trade held a hearing on daily fantasy sports and sports betting in May 2016, but it resulted in no further action regarding the industry. (NCSL submitted a document for the record for the hearing in support of the sovereignty of states to regulate and tax daily fantasy sports).

One piece of federal legislation that could have a direct impact on fantasy sports is the Professional and Amateur Sports Protection Act (PASPA). This law makes wagering on sports generally illegal throughout the country, with exceptions for Nevada’s sports wagering business and a few states’ sports lotteries that were already in operation. PASPA is currently being argued as unconstitutional by the state of New Jersey in Christie v. National Collegiate Athletic Association. The State and Local Legal Center, which provides assistance to the state and local governments in connection with Supreme Court litigation, filed an amicus brief in support of New Jersey.

State Action

The daily fantasy sports industry has been around for over seven years, but it wasn’t until a $200 million advertising blitz in 2015 that the two leading fantasy sports operators, DraftKings and FanDuel, became household names. This move helped these companies gain prominence and produce more players, and it caught the attention of state lawmakers and attorneys general. Without specific statutes to clarify the law on the fantasy sports industry, many DFS businesses began operating in a legal grey area. States and territories relied on court precedent, attorneys general opinions, public statements or other laws to determine or predict the legality of fantasy sports in their jurisdictions.

Since 2015, 43 states have introduced legislation relating to fantasy sports. Nineteen states have enacted laws to legalize paid-entry fantasy sports, generally with two goals in mind: first, to create legal clarity, regulations and safeguards for their

Did You Know?

• Daily fantasy sports (DFS) operators are active in 41 states, while only 19 states have statutes formally legalizing it.

• The National Collegiate Athletics Association (NCAA) has been critical of daily fantasy sports, and many bills regulating DFS have specifically blocked operators from offering the contests for college football, college basketball or amateur sporting events.

• Disney launched a fantasy league game for ABC’s “Bachelorette” show in 2017 to help broaden the reach to women. The two Bachelorette Fantasy League games offered so far were played by more than 700,000 users, 75 percent of whom were women.
residents, and second, to raise revenue.

Regulations include setting a minimum age for players, preventing DFS operator employees from participating in contests, segregating player funds from operational funds, and establishing a state agency to oversee the industry. At the urging of groups like the National Collegiate Athletics Association (NCAA), some states also prohibited contests for amateur athletic events, including college sports. Several states also set up special task forces or commissions to study and review various aspects of fantasy sports and DFS, including economic development, consumer protection and taxation.

As states continue to address budget shortfalls across the country, many are looking to expand their tax bases, especially in digital commerce, services and excise taxes. Of the 19 states that have legalized daily fantasy sports to date, 10 have imposed operating fees, ranging from $5,000 for three years to $50,000 annually, and 10 states approved taxing operators’ revenue generated within the state.

Those who believe taxing daily fantasy sports companies will create meaningful revenue for their budgets may be in for a rude awakening. While over 59 million people play, the number of people playing paid-entry daily fantasy sports is much smaller. In addition, the revenue that is taxed is only a fraction of the “handle”—the amount operators collect in entry fees.

States that have legalized this new industry are still in the early stages of assessing its fiscal impact. Pennsylvania, one of the largest states to legalize paid-entry fantasy sports, released a House fiscal note estimating the tax will generate over $500,000 in the remaining three months of its fiscal year.

While the DFS industry is still in its infancy, what it ultimately becomes remains to be seen. But as the possibility of legal sports betting across the nation looms on the horizon, it is all but certain that gaming in America will continue to evolve in the 21st century.