

THE COMMONWEALTH OF MASSACHUSETTS



White Paper on Daily Fantasy Sports

MASSACHUSETTS GAMING COMMISSION

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JANUARY 11, 2016

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January 11, 2016

A Letter from the Chairman:

With the advent of the NFL Football season and its advertising in the Fall of 2015, coupled with the widely-distributed story of a DraftKings insider making big money on a competitor's site, the relatively new activity of Daily Fantasy Sports (DFS) exploded into the public's consciousness. Gaming regulators, Attorneys General, and Legislatures across the country suddenly confronted the complex questions about the legality of DFS, the definition of gambling, the significance of skill vs. chance, and the overall muddled state of societal views of gambling and the equally muddled state of much of its regulatory infrastructure.

Massachusetts was particularly caught up in this new controversy due to the existence of one of the leading DFS companies, DraftKings, being headquartered in Boston, the participation of the Kraft family in DFS, and the Attorney General's effort to sort through the legal thicket to focus on critical consumer protection issues. In the course of this public debate, the Governor, the Speaker of the House, and the Senate President all suggested, at least casually, that it might be helpful if the Gaming Commission were to offer its views on these issues. It is absolutely clear that the Gaming Commission, at this point, has no authority whatsoever either to regulate (that authority rests principally with the Attorney General) or to set policy (that authority rests with the Legislature) concerning DFS. The Gaming Commission *does* have considerable experience in launching a new gaming industry in Massachusetts and in considering many of the complicated and nuanced issues pertaining to gaming regulation. Further, the Commission has a responsibility under its enabling legislation to help protect the interests of the Lottery, and has a clear interest in rationalizing the gaming environment in which its casino licensees operate.



Massachusetts Gaming Commission

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For all of these reasons, the Commission has decided to publish this White Paper, offering our thoughts on a range of issues the Legislature will likely confront as it comes to grips with the challenge of regulating DFS, and perhaps other online (also referred to as “Internet-based,” or “remote”) gaming. The Commission expects that these issues will likely include at least the following:

- Not so much the issue of *whether* DFS is legal under existing relevant law, but rather whether DFS *should* be legal.
- If the Legislature determines DFS should be legal, should it be regulated?
- If the Legislature determines that DFS should be regulated, what are the critical issues that need to be addressed by that regulation?
- As the Legislature determines what issues need to be addressed, it will likely consider what regulatory structure is appropriate, ranging from consumer protection laws, the regulatory style of the Department of Public Licensure (hairdressers, plumbers, etc.) or the full agency-led regulation like the Division of Banks, the Division of Insurance or the Gaming Commission.

Most of this Paper will be focused on the specific challenges of DFS. However, the Commission is very aware that while today DFS is the hot new Internet-based gaming, in past years it was online poker, and next year it may well be eSports. Online gaming technologies are proliferating at an ever faster pace, and new games can be deployed to a mass market in a matter of weeks. The last section of this Paper will suggest the possibility of the Legislature establishing a regulatory environment which is applicable to all online gaming technologies, assigning that regulatory structure to an agency for implementation, and leaving the daily work of drafting and adapting regulation of new gaming types to the regulatory agency that can be nimble and flexible in responding to technological gaming innovations.

An alternative approach is exemplified by the prodigious work the Legislature did to draft the Gaming Commission’s enabling Legislation, Chapter 23K. This Legislation, years in development, established clear societal values, regulatory priorities, many highly directive regulatory parameters, and a host of regulatory innovations that have made much of Massachusetts casino regulation a model for other jurisdictions. It is probably impractical for the Legislature to do similar work for each new type of gaming; however, it may be that its comprehensive work in Chapter 23K has



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already established the primary values and regulatory priorities that will need to be adapted to any new type of gaming.

In preparation for drafting this White Paper, the Commission (led by Commissioner Gayle Cameron, Staff Attorney Justin Stempeck and Director of Licensing Paul Connelly; Stempeck and Connelly served as lead authors of this Paper, along with Commissioner Lloyd Macdonald and former Commissioner Jim McHugh) held several information-gathering sessions with the DFS industry and experts, culminating in an extraordinary day-long forum on DFS and online gaming on December 10, 2015, that informed much of this Paper. The video and transcript of that Forum can be found at <http://massgaming.com/news-events/article/daily-fantasy-sports-educational-forum-december-10-2015-2/>.

I hope that the contents of this White Paper will be helpful.

A handwritten signature in black ink, appearing to read "Stephen Crosby", with a stylized flourish at the end.

Stephen P. Crosby
Chairman



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EXECUTIVE SUMMARY

Daily Fantasy Sports (DFS) first started in 2007. This variant of fantasy sports offers a condensed version of the season-long fantasy experience, providing for the drafting of a team and participation in weekly or daily contests. The most popular DFS sport is football, followed by baseball, racing, basketball and hockey. Fantasy golf is also a popular product and is quickly gaining in popularity.

With the advent of the NFL Football Season and its advertising in the Fall of 2015, coupled with the widely-distributed story of a DraftKings insider making big money on a competitor's site, DFS exploded into the public's consciousness. Gaming regulators, Attorneys General, and Legislatures across the country suddenly confronted the complex questions about the legality of DFS, the definition of gambling, the significance of skill versus chance, and the overall muddled state of societal views of gambling and the equally muddled state of much of its regulatory infrastructure. Pursuant to these events, and with encouragement of political leaders on Beacon Hill, the Massachusetts Gaming Commission (MGC) has decided to publish this White Paper, offering our thoughts on a range of issues the Legislature will likely confront as it comes to grips with the challenge of regulating DFS, and perhaps other online (also referred to as "internet-based," or "remote") gaming. The Commission expects that these issues will likely include at least the following:

- Not so much the issue of *whether* DFS is legal under existing relevant law, but rather whether DFS *should* be legal.
- If the Legislature determines DFS should be legal, should it be regulated?
- If the Legislature determines that DFS should be regulated, what are the critical issues that need to be addressed by that regulation?
- As the Legislature determines what issues need to be addressed, it will likely consider what regulatory structure is appropriate, ranging from consumer protection laws, the regulatory style of the Department of Public Licensure (hairdressers, plumbers, etc.) or the full agency-led regulation like the Division of Banks, the Division of Insurance or the Gaming Commission.

The last section of this paper will suggest the possibility of the Legislature establishing a regulatory environment which is applicable to all online gaming technologies, assigning that regulatory structure to an agency for implementation, and leaving the daily work of drafting and adapting regulation of new gaming types to the regulatory agency that can be nimble and flexible in responding to technological gaming innovations.

One approach to regulating DFS and other Internet-based gaming is exemplified by the prodigious work the Legislature did to draft the Gaming Commission's enabling Legislation, Chapter 23K. This Legislation, years in development, established clear societal values, regulatory priorities, many highly directive regulatory parameters, and a host of regulatory innovations that have made much of Massachusetts' casino regulation a model for other jurisdictions. It is probably impractical for the Legislature to do similar work for each new type of gaming; however, it may be that its comprehensive work in Chapter 23K has already established the primary values and regulatory priorities that will need to be adapted to any new type of gaming.

Massachusetts is in unsettled legal territory with respect to DFS as there are no statutes or legal decisions that directly address the topic. Without otherwise addressing DFS under the current laws of the Commonwealth, Attorney General Healey recently promulgated comprehensive draft consumer protection regulations to reduce or eliminate the risk of economic harm to vulnerable players and to promote the games' transparency. While these proposed regulations will mitigate many of the potential harms of DFS, the state Legislature possesses the singular power to clarify any remaining legal ambiguity with appropriate legislation.

From our own review of the gambling statutes currently in effect in the Commonwealth and from our review of the opinions of other interested parties, we believe that DFS does implicate certain provisions of existing civil and criminal statutes. However, while it could be construed that DFS is arguably illegal under existing Massachusetts law, the balance of Massachusetts law may make that reading illogical. See the discussion offered in detail in Section II, Legality of Daily Fantasy Sports.

In any case, a common concern repeated in the DFS industry by operators, players and vendors alike is a greater need for legal certainty. The real question for the Legislature is ultimately not "Is DFS legal?" but "Do we want DFS to be legal, and if so, under what conditions?" Nevertheless, we believe that before addressing that question, it is important that there be an understanding of the present legal framework of gaming in Massachusetts and at the federal level so that any legislative

solution here avoids conflict with existing laws, or intentionally amends those laws that otherwise would be in conflict with the Legislature's solution.

The Massachusetts statutes that present the greatest direct exposure to DFS operators, third party vendors and gaming participants are the statutes that make criminal the operation of betting pools, M.G.L. c. 271, §§ 16A and 17, and the holding of illegal lotteries, M.G.L. c. 271, § 7.

What makes the Massachusetts pooling statutes so potentially problematic for DFS is that the element of skill—so central to the DFS operator's defense to date—is irrelevant to the issue of culpability. That is because the statutes specifically reference a "trial or contest of skill" as the basis of an illegal pool. Accordingly, this language places DFS participants (operators, third party vendors and players) at risk.

The lottery statute poses challenges to DFS, as well, although not as directly as the betting pool statutes. The term "lottery" has been interpreted broadly by the courts to include any activities consisting of the following three elements: "(1) the payment of a price for (2) the possibility of winning a prize, depending upon (3) hazard or chance." See *Com. v. Stewart-Johnson*, 78 Mass. App. Ct. 592, 594 (2011), quoting, *Com. v. Lake*, 317 Mass. 264, 267 (1944). The running of lotteries outside of a "gaming establishment" is illegal under Massachusetts law and such lotteries are broadly defined in the statute:

Whoever sets up or promotes a lottery for money or other property of value, or by way of lottery disposes of any property of value, or under the pretext of a sale, gift or delivery of other property or of any right, privilege or thing whatever disposes of or offers or attempts to dispose of any property, with intent to make the disposal thereof dependent upon or connected with **chance** by lot, dice, numbers, game, hazard or other gambling device ... shall be punished by a fine ... or by imprisonment (*Emphasis added.*)

M.G.L. c. 271, § 7

This debate about skill versus chance is at the heart of the DraftKings – State of New York legal actions, and similar debates and lawsuits across the nation. In the Commission’s judgment, it would be worthwhile for the Legislature to consider whether it is in the public interest for DFS to be exposed to the uncertain reach of the lottery statute, or to the “skill” vs. “chance” distinction at all.

The federal statute that potentially presents the greatest constraints on state action to address DFS is the Professional and Amateur Sports Protection Act or “PASPA.” 28 U.S.C. § 3701 (1992). In simple layman’s terms, PASPA makes illegal (except in a few grandfathered states) essentially any state action that makes sports or sports-related betting legal. Thus, at first glance, PASPA may constrain the Legislature from any legislation that directly or indirectly permits or regulates DFS. While there appears to be little appetite for further PASPA challenges by those provided with a right of action under the statute, the lack of significant court interpretation of the statute, the inherent vagueness of the statutory terms and the pending *en banc* review in the Third Circuit of New Jersey’s most recent attempt to legalize sports betting, suggests a cautious approach to state action addressing DFS directly.

There is, however, an alternative approach for the Legislature to consider. Rather than trying to anticipate unfavorable outcomes, or trying to design Massachusetts public policy that accommodates a peculiar and vague federal statute, the Legislature might simply write legislation and regulations it believes appropriate for the people of Massachusetts, and let the others react as they see fit. Ultimately, clarification of federal law on this (and many other) aspects of gaming law will be required; clear and decisive state action may further that objective.

The Gaming Commission believes that the issue of “whether to regulate DFS” is largely settled.

After several years of a largely laissez-faire environment, there is a growing consensus amongst regulators, industry analysts and the DFS industry itself that some form of regulation is necessary not only to protect the interest of DFS players, but also to provide some clear guidelines and predictability to DFS operators. While cautious of the potential breadth of regulations, and fearful of a patchwork implementation across the country, the major DFS operators have all publicly recognized the need for government regulation to provide security to customers and operators alike. The majority of the debate in this area continues to focus on the form and extent of a future potential regulatory environment.

In the past, legislators and regulators typically approached the issue of gaming legality by asking the questions, “is it gambling?” and often “is it a game of skill or a game of chance?” As discussed in this paper, much of this analysis has been a residue of moral judgments initially asserted hundreds of years ago, and carried forward in many religious and ethical constructs, and the definitions of “gambling,” “skill” and “chance” have often been unclear at best. Even with these religious and ethical disapprovals, however, gambling of one sort or another—especially lotteries—has been approved and utilized by government jurisdictions and other institutions as a means of raising revenues and providing entertainment since at least the beginning of this Republic. And much more recently, the Legislature and the people of Massachusetts have emphatically endorsed many forms of gambling by way of the legalization of the Lottery and casinos.

We are left now with a public policy position that seems to assert that gambling is bad/illegal, except when it is not. And what makes it not bad/illegal is when the Legislature authorizes a regulatory framework and a public purpose for a particular kind of gambling. Generally speaking, we have largely come to accept gambling as a legitimate form of economic activity, entertainment and public or philanthropic revenue generation (even within the religious community) – under certain regulatory conditions.

Perhaps, as a consequence of profound changes in public values and public policy, the challenge for the Legislature about DFS and other internet-based gaming is to define gambling clearly and carefully, and then regulate accordingly. For example, the Legislature might use this definition: “Is this economic activity characterized by a payment by a player for an opportunity to win an award based on the outcome of a future event, which is not otherwise regulated?”

The Commonwealth routinely regulates most economic activity, at some level of intensity, looking into the nature of that activity to determine whether and how to regulate. In this case, it may be helpful to define in law the specific features that might be considered gambling, to serve as the tripwire for a greater than normal degree of regulation. If the proposed economic activity has these defining features, it will be considered gambling, and then the checkered history of gambling, the continuing public ambivalence about gambling activities, and long established public policy, suggest a number of key topic areas that may require regulatory consideration.

The following issues and potential remedies, presented across five, broad policy areas, represent a starting point for consideration of a regulatory schema. (These issues are also presented in a table format in Section III Issues Requiring Regulation.)

Know your Customer: Ensuring that players are of legal age and are playing in a jurisdiction where DFS play is allowed. Ensuring that DFS operators can uniquely and accurately identify each and every DFS player.

DFS Player Protection: Ensuring that players' funds are properly protected, and that players understand the nature of the games, the risks involved and have access to tools and resources if they feel they have a problem.

Technical Security: Ensuring that the wealth of personal information regarding customers is protected, the system cannot be manipulated to any player's advantage, and all user activity data is retained for auditing and research purposes.

Suitability and Licensure: Ensuring that regulators know the principals involved in DFS operations, and that there is a level of investment that increases the costs of non-compliance.

Impact on Real-World Sports: Ensuring that the relationship between DFS and the sports for which it provides contests does not adversely affect the perception (or reality) of fair play.

There are multiple regulatory models that could be employed to address the issues outlined above. The Attorney General's proposed regulations consider the most important issues of concern and provide consumers with a powerful tool to address their concerns and grievances. This tool, however, necessitates that an aggrieved consumer or law enforcement agency seek remedy which for many may be too costly or time consuming to pursue, and which in any case provides only a very random method of enforcement. An appropriately robust regulatory structure would consider how to work in concert with the Attorney General's proposed consumer protection regulations to address these same concerns *prospectively*, so that issues are detected and addressed, or avoided altogether without the need for consumer action.

In considering the appropriate kind of regulatory scheme for DFS and other on-line gaming, certain principles are worth bearing in mind:

- The scheme must be commercially viable
- The scheme must be technologically feasible
- The scheme should attempt to balance the “problem solved” with the “cost increased”
- The scheme should be “risk-based,” balancing the risk and seriousness of the problem with the cost and imposition of the solution

Whatever the outcome, careful thought should be afforded to the design of the regulatory approach, as many other jurisdictions may look to the first successful model for guidance. Furthermore, the DFS industry’s present urgent desire for a consistent regulatory approach will probably mitigate resistance that might otherwise exist to implementation of a prompt, comprehensive, “smart” model.

The discussion thus far has focused primarily on DFS. However, DFS is only one form of Internet gaming activity that the Commonwealth is likely to encounter in both the near and the long term. Internet gaming (also referred to as “online” or “remote” gaming) offers a dizzying and constantly expanding variety of games including on-line casino games, sports betting, eSports, social gaming, skill-based games, and prediction markets (all discussed more fully in Section V, The Proliferation of Internet Gaming.) Any new regulatory effort for just one of these types of games will surely beg the question of how to handle the others. A regulatory strategy that is broad enough and flexible enough to adapt to any and all of these proliferating games may be worth serious consideration.

As recent history and litigation demonstrate, it is not enough – indeed, it is frequently not fruitful – simply to ask whether a new form of Internet activity involving payment of money for future rewards constitutes “gambling”. The real question is how to determine whether a new Internet activity involving payment of money in return for future rewards ought to be regulated and, if so, how and by whom. Not all such activity necessarily requires regulation. Even when regulation is required, regulations and the regulatory framework must be of the right size, i.e., neither so onerous that it stifles positive economic activity nor so lax that it fails to protect the public interest.

One approach for the Legislature to consider is to recognize that because Internet gaming activity is unique, quickly deployed and highly malleable, regulation ought to be vested in a single, nimble Internet gaming regulatory body. This approach would require new legislation, but the regulatory body could be one that currently exists or one that the Legislature creates. Such omnibus on-line gaming regulatory legislation would establish the Commonwealth's overriding public policy objectives and regulatory principles, presumably including the principles embodied in existing horse racing, gaming and lottery legislation enumerated in Section III of this Paper. Minimally, such legislation would direct that organized crime and individuals with criminal backgrounds have no operational control over the gaming activity, that players are protected from unfair or deceptive practices when they engage in the gaming activity, that operators of the activity take appropriate steps to mitigate any adverse consequences the activity may produce, and that the activity produces economic benefits for Massachusetts. The economic benefits may come through taxation of the activity at a rate the Legislature determines but also through encouragement of Massachusetts job creation and economic development.

If such an omnibus online gaming regulatory body were created, it would be important to give it jurisdiction also over all Internet-based (or "online" or "remote") economic activity in which a person stakes or risks something of value on the outcome of a future event, whether that outcome is dependent on chance, the individual's skill or a combination of both. So formulated, the regulatory body's jurisdiction would be broad enough to invest it with the power to look at all Internet gaming activity, determine whether any form of regulation of that activity is necessary and, if it is, create "right-sized" regulations to deal with it, pursuant to the public policy objectives and regulatory principles in the Legislature-promulgated enabling legislation.

To be sure, an agency with a broad mandate of that kind and description would have considerable power to affect what could become a broad swath of economic activity on the Internet. Accordingly, legislative oversight, even if in arrears, would be highly desirable. But with that broad mandate and developed expertise, such an agency would be prepared to provide the Legislature and the citizens of Massachusetts with informed regulatory measures, promptly, economically, and thoughtfully, to avoid clear pitfalls while promoting economic growth in a dynamic arena.

I. THE EVOLUTION OF DAILY FANTASY SPORTS

This section will briefly address the history of fantasy sports as well as the recent development of daily fantasy sports or “DFS” in order to provide some perspective on the rapidly evolving market for these businesses.

A. History

Fantasy sports are largely understood to have started with a 1980 “Rotisserie” Baseball League (named for the New York Restaurant where the draft was held; *La Rotisserie Francaise*). Under the rules of this first league, each participant used an imaginary budget to bid on various baseball players at a simulated auction in order to draft a team. Over the course of the baseball season, the league participants kept track of various statistics of their players, scoring points based on the performance of their players, with the participant who scored the most points at the end of the season winning a cash prize.

Early fantasy sports aficionados started playing Rotisserie-style fantasy baseball and the game accumulated a small but devoted following. As the game evolved, players suggested new rules (including weekly head-to-head format, keeper leagues¹, and others) but largely adhered to the core premise.² Over time, the game format migrated outside of baseball to other professional sports. Popularity of the game spiked in conjunction with the mid 1990’s Internet boom likely due to the automation of scoring contests, the ready availability of eager contest participants and easy access to sports news and information. In conjunction with the creation of numerous new fantasy sports sites came fantasy sports *support* sites, offering player insights and recommendations on drafting the strongest team.

¹ In a “keeper” league, depending upon the rules, anywhere from one player to an entire team is retained from one sports season to the next.

² One of the primary distinctions in fantasy sports leagues comes in the initial allocation of players. Although the original format featured an auction draft, another popular variant is the “snake draft,” where participants are randomly assigned a number designating their pick position in the draft. During the draft the participant that picked first in round one goes last in round two and the participant that picked last in round one goes first in round two.

B. Advent of Daily Fantasy Sports

Daily Fantasy Sports or “DFS” first started in 2007. This variant of fantasy sports offers a condensed version of the season-long fantasy experience, providing for the drafting of a team and participation in weekly or daily contests. The most popular of DFS sport is football, followed by baseball, racing, basketball and hockey. Fantasy golf is also a popular product and is quickly gaining in popularity.

The current DFS landscape is dominated by two companies: DraftKings and FanDuel, which together account for 85-95% of the market.³ Both companies offer a similar experience, allowing participants to draft players using a salary cap auction. In that format all participants start with the same amount of imaginary funds to use to draft players to fill their team roster. Real-world players are assigned fictitious “salaries” by the DFS site operators, based on a number of known factors (player past performance, weather, team match ups, etc.) and certain factors unknown to participants. Under this format participants are allowed to draft the same players, as long as they do not exceed their assigned salary cap. Each imaginary roster accumulates various points over the course of the contest based on the real world performance of the professional sports players and at the end of the contest period (either a week or a day), the points are tallied and the results are reported.⁴

DFS sites offer a variety of contest types including private league, head-to-head, 50/50 and guaranteed prize pools. Private leagues allow participants to create an entire league where participation is limited by invitation of the league creator. Head-to-head match ups are one-on-one contests between two players. 50/50 leagues involve a large pool of people where the participants in the top half of the standings win and those in the bottom half lose. These contests often allow for the potential to multiply winnings based on how high in the percentile rankings a participant reaches. Guaranteed prize pools involve a contest for an operator guaranteed sum (for example \$1 million), which will be paid out to the winner whether contest entry fees meet that sum or not. In the event that entry fees fail to fully fund the guaranteed contest, the DFS operator will make up the difference in order to fund the contest. The operator typically retains 8-10% of the total entry fees from each DFS contest, similar to the “vig” in pari-mutuel betting, or the “rake” in casino poker.

³ The remaining market share is split between approximately 18 other smaller companies.

⁴ All of these functions, from drafting a team to checking the real time score of a contest, can also be completed using a paired smartphone application.

The current DFS market is estimated to be 3-4 million players. Many news stories have conflated this number with the significantly greater figure representing all players of fantasy sports generally (which would include season long fantasy sports players). The majority of DFS players are white males in their mid-twenties to mid-thirties. Eilers Research CEO Todd Eilers estimates “that daily games will generate around \$2.6 billion in entry fees this year and grow 41% annually, reaching \$14.4 billion in 2020.” Notably, this projection was made before the DFS legal backlash that occurred this past fall and it is unknown what effect this slew of lawsuits and law enforcement investigations will have on these projections.

II. LEGALITY OF DAILY FANTASY SPORTS

Massachusetts is in unsettled legal territory with respect to DFS as there are no statutes or legal decisions that directly address the topic. Without otherwise addressing DFS under the current laws of the Commonwealth, Attorney General Healey recently promulgated comprehensive draft consumer protection regulations to reduce or eliminate the risk of economic harm to vulnerable players and to promote the games' transparency. While these proposed regulations will mitigate many of the potential harms of DFS, the state Legislature possesses the singular power to clarify any remaining legal ambiguity with appropriate legislation.

From our own review of the gambling statutes currently in effect in the Commonwealth and from our review of the opinions of interested others⁵, we believe that DFS does implicate certain provisions of existing civil and criminal statutes. However, while it could be argued that DFS is illegal under existing Massachusetts law, the balance of Massachusetts law may make that reading illogical.

In any case, a common concern repeated in the DFS industry by operators, players and vendors alike is a greater need for legal certainty. The real question for the Legislature is ultimately not "Is DFS legal?" but "Do we want DFS to be legal, and if so, under what conditions?" Nevertheless, we believe that before addressing that question, it is important that there be an understanding of the legal framework of gaming in Massachusetts and at the federal level so that any legislative solution here avoids conflict with existing laws, or intentionally amends those laws that otherwise would be in conflict with the Legislature's solution.

⁵ At the December 10, 2015 DFS Forum the issue of DFS' relationship to illegal sports betting was addressed by several national experts in attendance. Also, the Commission's legal staff solicited and received comprehensive legal memoranda on the subject from DraftKing's counsel. (Senior personnel from DraftKings and FanDuel and their counsel were also on several of the panels at the Forum.) The Forum was live-streamed, and a complete video record and transcript of the Forum is available on the Commission's website.

A. Massachusetts Statutes Posing Issues for DFS

Massachusetts addresses illegal gaming through a number of criminal and related civil statutes including, but not limited to, statutes on the operation of an illegal gaming establishment,⁶ the recovery of gaming losses,⁷ the loaning of money for purposes of gaming,⁸ gaming establishments as a public nuisance⁹, rights of entry to seize implements and materials of a “common gaming house”¹⁰, forfeiture of gambling devices¹¹, keeping a “common gaming house” or being knowingly present therein¹² and the operation of a bet-placing operation;¹³ amongst others.

In Massachusetts “the word ‘game’ is very comprehensive and embraces any contrivance or institution which has for its object the furnishing of sport, recreation or amusement. ‘Gaming for money or other property’ is illegal.” Com. v. Theatre Adver. Co., 286 Mass. 405, 411 (1934). In the statute that provides a glossary of definitions for subsequent reference in the General Laws, “illegal gaming” is defined in as any “banking or percentage game played with cards, dice, tiles or dominoes, or an electronic, electrical or mechanical device or machine for money, property, checks, credit or any representative of value, but excluding [the state sanctioned lottery, casinos authorized by the Gaming Commission enabling act, horse and dog racing, bingo and charitable gaming].” M.G.L. c. 4, § 7. Although the statute is definitional only and does not have any affirmative provisions for criminal or civil consequences, the state’s Supreme Judicial Court cited the statute in holding that “[i]t is settled that the buying or selling of pools or the registering of bets is illegal gaming in this commonwealth,”. *Sullivan v. Vorenberg*, 241 Mass. 319, 321 (1922).¹⁴

The statutes that present the greatest direct exposure to DFS operators, third party vendors and gaming participants are the statutes that make criminal the operation of betting pools, M.G.L. c. 271, §§ 16A and 17, and the holding of illegal lotteries, M.G.L. c. 271, § 7.

⁶ M.G.L. c. 137, § 2.

⁷ M.G.L. c. 137, § 1.

⁸ M.G.L. c. 137, § 3.

⁹ M.G.L. c. 139, § 14

¹⁰ M.G.L. c. 271, § 23

¹¹ M.G.L. c. 271, § 5A

¹² M.G.L. c. 271, § 5

¹³ M.G.L. c. 271, § 17.

¹⁴ There is no specific statute criminalizing running a “banking or percentage game” even if such an operation is labeled “illegal gaming” under § 17.

1. Betting Pools

M.G.L. c. 271 § 17 provides that it is a felony for one who possesses an “apparatus, books or any device...for buying or selling pools, upon the result of a trial or contest of skill, speed or endurance of man, beast, bird or machine, or upon the result of a game....” Section 16A makes it similarly illegal for one who “organizes, supervises, manages or finances ... the illegal buying or selling of [such] pools.”

The Supreme Judicial Court in *Commonwealth v. Sullivan*, addressed the meaning of a betting pool and how a betting pool works:

A pool has been defined as 'a combination of stakes the money derived from which was to go to the winner.' . . . This does not mean, however, that all the money derived from the combination of stakes must go to the winner. Commonly the man who runs the pool makes something out of the transaction. It is enough to constitute the criminal offense if there is a combination of stakes a part of which is to go to the winner. . . . [It] is enough if the proceeds [advanced by the players] constituted a fund out of which the so-called prizes--in fact the proceeds of the pool--were paid to the winners in the game of chance.¹⁵

218 Mass. 281, 283 (1914) (citing the definition articulated by Oliver Wendell Holmes in *Commonwealth v. Ferry*, 146 Mass. 203, 208 (1888)).

¹⁵ In this regard, it is worth noting that the CEO of DraftKings, Jason Robbins, was quoted in a Reddit post July 26, 2012, as saying “For example, when anyone on my fantasy team hits a home run in real life, I get points on my team. The person with the most points at the end of all the games, wins. In our case, you win the total wager amount of all the people who had teams in that contest. If there were 10 people, and each put in \$10, you’d win \$100 (*minus 10% which goes to us*)”. (Emphasis added).

The Court described the activity at issue in *Sullivan* in the following terms:

There was evidence tending to show that the defendants kept the rooms and there kept and sold, for twenty-five cents each, books entitled, 'American and National League Baseball Schedule and Record Book.' The book was exhibited in evidence and is described in the record as 'containing many advertisements and a schedule of dates when and places where baseball games were to be played by the various clubs belonging to the American and National Leagues together with some other information.' One page contained two coupons to be filled out in duplicate 'by writing in the names of the baseball clubs which the contestant believed would score the greatest number of runs on each day of the following week.' One coupon was to be given to one of the defendants and the other kept by the contestant. The names of six different baseball teams could be used, but the name of one could not be used twice during the same week. Prizes of considerable amounts were offered. . . . Whether the aggregate of the prizes constituted the entire pool does not appear in the evidence and is of no consequence.

Sullivan further defines a “bet” as “the hazard of money or property upon an incident by which one or both parties stand to lose or win by chance.”¹⁶ *Id.* “For one to have placed a “bet,” he must have taken a risk on the uncertain outcome of a particular event and, depending on the outcome, he must be entitled to receive payment from another.” *Com. v. Sousa*, 33 Mass. App. Ct. 433, 437 (1992)

The typical DFS contest involves numerous participants paying their entry fees to a company, the company taking a percentage of the total entry fees and the winner being paid from the company's coffers. Such contests bear more than passing resemblance to the betting pools found to be illegal in *Sullivan*. In this respect, the Commission finds significant that the Nevada Gaming Control Board recently found DFS to constitute betting pools under Nevada's law and thus subject to mandatory regulation as other forms of gambling are there.

¹⁶ This definition is similar to the definition of “wager” applied by the Nevada attorney general. In Nevada, a wager is “a sum of money or representative of value that is risked on an occurrence for which the outcome is uncertain.” *See Nev. Rev. Stat. Ann.* 463.01962.

What makes the Massachusetts pooling statutes so potentially problematic for DFS is that the element of skill—so central to the DFS operator’s defense to date—is irrelevant to the issue of culpability. That is because the statutes reference a “trial or contest of skill” as the basis of an illegal pool. Accordingly, this language places DFS participants (operators, third party vendors and players) at risk.¹⁷

The pooling statutes, in particular, should be addressed to determine whether they should be amended.

2. Lotteries

The lottery statute poses challenges to DFS, as well, although not as directly as the betting pool statutes. The term “lottery” has been interpreted broadly by the courts to include any activities consisting of the following three elements: “(1) the payment of a price for (2) the possibility of winning a prize, depending upon (3) hazard or chance.” See *Com. v. Stewart-Johnson*, 78 Mass. App. Ct. 592, 594 (2011), quoting, *Com. v. Lake*, 317 Mass. 264, 267 (1944). The running of lotteries outside of a “gaming establishment” is illegal under Massachusetts law and such lotteries are broadly defined in the statute:

Whoever sets up or promotes a lottery for money or other property of value, or by way of lottery disposes of any property of value, or under the pretext of a sale, gift or delivery of other property or of any right, privilege or thing whatever disposes of or offers or attempts to dispose of any property, with intent to make the disposal thereof dependent upon or connected with chance by lot, dice, numbers, game, hazard or other gambling device ... shall be punished by a fine ... or by imprisonment

M.G.L. c. 271, § 7.¹⁸

¹⁷ If DFS were to be found to comprise an illegal betting pool, then by operation of the other gaming-related statutes referenced above, the parties could be prosecuted for operating an “illegal gaming establishment” and being “present” therein; the operation could be declared a “public nuisance” and shut down, and the equipment at the premises and the proceeds generated by the contests could be subject to civil forfeiture. Any person or organization providing goods and services knowing the nature of the DFS games could also be exposed to liability as an accessory.

¹⁸ This statute has been widely used as a catch-all for other types of illegal gambling:

In order to set chance-based endeavors apart from other contests that rest on the skill of participants, the Supreme Judicial Court adopted the “dominant factor test.” The SJC has stated:

Where the game contains elements both of chance and of skill, in order to render the laws against lotteries effectual to combat the evils at which they are aimed, it has been found necessary to draw a compromise line between the two elements, with the result that by the weight of authority a game is now considered a lottery if the element of chance predominates and not a lottery if the element of skill predominates.

Com. v. Lake, 317 Mass. 264, 267 (1944); see also *Com. v. Plisner*, 295 Mass 457, 464 (1936).

Massachusetts cases evaluating the chance versus skill balance have looked at a number of different factors as set forth below:

In *Plisner*, the Court found that a machine where a player operated a toy crane to attempt to pick prizes was more chance than skill (and thus a lottery) where the players’ only ability to manipulate the crane was to set the area where it would descend and where the player had no ability to influence the manner or strength by which the crane closed its claw on a potential prize. 295 Mass. at 244.

In *Com. v. Theatre Advertising Co., Inc.*, 286 Mass. 405, 410 (1934), the court found that a game called “Beano,” consisting of a combination of darts and bingo, involved more chance than skill and thus constituted illegal gaming.

Over time, “lottery” has become used as shorthand for a wide variety of gambling practices deemed to be prohibited by the statute. Such practices extend significantly beyond the narrowest sense of the term (the sale of chances that a number selected by a player will match one chosen in a random drawing). Thus, for example, a pinball game with a cash prize has been viewed as a “lottery” within the meaning of the statute.

Com. v. Stewart-Johnson, 78 Mass. App. Ct. 592, 595, (2011), citing *Com. v. Macomber*, 333 Mass. 298 (1955).

Similarly, in *Lake* the court examined a machine that players would pay to use to attempt to win prizes. After paying, the player could press a button to cause a mechanical arm to swing out in an attempt to push various prizes into a hole in the center of a rotating circle. The defendant argued that the machine did not constitute a lottery where success was based on the skill of the player. The court reasoned that even if it was possible to become skilled enough in the machine to outweigh the chance involved that “in determining which element predominates, where the game is not one of pure skill or of pure chance, some courts have held, we think rightly, that it is permissible in appropriate instances to look beyond the bare mechanics of the game itself and to consider whether as actually played by the people who actually play it chance or skill is the prevailing factor.” *Id.* at 925. Ultimately, the court explained that the determination of whether the game was more one of skill or chance was to be left to the jury.

In *U.S. v. Marder*, 48 F.3d 564 (1st Cir. 1995), the First Circuit examined the chance versus skill argument in the context of video poker machines while applying Massachusetts law. The court found that chance predominated and that the jury could lawfully find that the defendant was operating an illegal lottery despite recognizing that there was some skill involved in a player choosing which cards to discard from any given hand. The court identified a number of considerations as material to the dominant factor calculus, including: the short amount of time that players were permitted to play a hand, the relative lack of normal poker skills in play, the profit that the operator made and the fact that “there were a great many more losers than winners.”

To date, no Massachusetts case has addressed whether season-long fantasy sports or DFS would constitute a “lottery” as in the examples set forth above. The cited cases all involved analyzing chance versus skill where the individual playing the game had a direct effect on the outcome of the game (i.e., personally operating a crane, choosing cards or throwing darts). These examples stand in contrast to DFS where the player’s skill is exercised only in choosing the roster, as the player has no ability to control the final outcome of the sporting events. DFS operators have consistently argued that theirs is a skill-based game and that they possess studies to prove unequivocally that skill trumps chance in their contests. This position has been extensively argued in the recent filings in New York by both DraftKings and FanDuel, and it was a recurrent theme in the materials submitted to the Commission staff by counsel for DraftKings.

The dominant factor test reduces the exposure that DFS operators have under the lottery statute, but ultimately, if a criminal charge were brought, the decision as to liability would be a jury issue. While a DFS players' skill can significantly affect the outcome of the contests, the reality is that no one knows who wins or loses until the last game (the athletes in which are the subject of the DFS contest) is concluded. And no one participating in the contest has control over the athletes whose performance ultimately drive the outcome of the DFS matches.

3. Evolution of Perspectives on "Skill vs. Chance"

This discussion of lotteries emphasizes the legal distinction between games of skill and games of chance—a tortured distinction presently being debated and litigated across the country. The underlying premise of this distinction is the notion that for some reason "games" of "chance" are bad, while "games" of "skill" are not – or at least are less so.

The Commission suggests that it may be time to assess the significance of this distinction, and to consider eliminating it from the legal discussion of gaming or gambling legality.

While there have been many different rationales for opposing gambling, and while philosophers and religions have historically differed on the degree of disapproval, the dominant disapproval in the United States seems to have grown out of a largely Protestant,¹⁹ than Puritan-imposed disapproval of earning something for nothing—of earning fortune by mere *chance*:

- "During the nineteenth century, morality arguments against gambling took center stage in the debate. Reformers pointed to gambling as an immoral activity engaged in by flouters of the Puritan work ethic, people who wanted to obtain something of value without contributing any work." "Regulatory Public Morals and Private Markets", Christine Hurst, Boston University Law Review, Vol 86.
- "Gambling, as a means of acquiring material gain *by chance* and at the neighbor's expense is a menace to personal character and social morality." United Methodist Church Book of Resolutions.

¹⁹"Some religious groups oppose all forms of gambling, continuing a tradition of moral criticism that has stemmed primarily from organized Protestantism (Weber; 1958. Downs et al, 1976; Ellison and Nyboten, 1999)." "Gambling Against the State," Cosgrove and Keassen, *Current Sociology*, September 2001, Vol. 49

- “Gambling is essentially the redistribution of a people’s wealth according to *chance* rather than according to the receiver’s contribution to society” American Baptist Convention, 1959.
- “Whatever encourages men to take from one another without giving value in return serves the cause of Satan. Gambling is a game *of chance* that takes without giving value in return. Gambling puts money or other things of value into a pool and then redistributes it on the basis of a roll of the dice, a spin of the wheel, or a drawing of a number. Nothing of value is produced in the process.” “Gambling-Morally Wrong and Politically Unwise,” Elder Dallin H. Oaks of the Quorum of Twelve, Church of Jesus Christ of the Latter-day Saints, January 1987.
(*Emphasis added.*)

This profound disapproval of games of chance was woven into many state’s laws and regulations, including Massachusetts, as seen in the discussion of lotteries above. A consequence of legislating this moral judgement has been the legal contortions of many forms of betting to demonstrate their reliance on skill, as opposed to chance. As Seth Stevenson wrote in *Slate*, on September 29, 2015, “The broader critique of daily fantasy betting is an older and more traditional one: that fantasy sports play is gambling, and gambling is bad. But the fact that some players consistently win demonstrates that if anything can be considered a game of skill – the technical loophole under which these forms of betting are considered legal—it’s fantasy sports.” Seth Stevenson, Think of the Children! The Moral Panic Over Fantasy Sports Betting is Misguided (Sept. 29, 2015), http://www.slate.com/articles/sports/sports_nut/2015/09/draftkings_and_fanduel_the_moral_panic_over_fantasy_sports_betting_is_misguided.html

This debate about skill versus chance is at the heart of the DraftKings – State of New York legal actions, and similar debates and lawsuits across the nation. In the Commission’s judgment, it would be worthwhile for the Legislature to consider whether it is in the public interest for DFS to be exposed to the uncertain reach of the lottery statute, or to the “skill” versus “chance” distinction at all.²⁰

²⁰ At the Commission’s December 10th DFS forum, three national gambling law experts on a panel were asked to comment as to the difference, if any, between “sports betting” and DFS. Their responses varied, but there was consensus that while DFS is significantly more complex than conventional sports betting and that DFS is a “head-to-head” contest as opposed to a competition against “the house”, the “connective tissue” binding the two were: (a) the payment of something of value; (b) with the payment made in the hope of winning a prize, and (c) the dependence of the award on the outcome of a sporting event or of the performance of athletes at such a sporting event over which the player had no control. The

B. Professional and Amateur Sports Protection Act (PASPA)

The federal statute that potentially presents the greatest constraint to state action to address DFS is the Professional and Amateur Sports Protection Act (PASPA) 28 U.S.C. § 3701 (1992). In simple layman's terms, PASPA makes illegal (except in a few grandfathered states) essentially any state action that makes sports or sports-related betting legal. Thus, at first glance, PASPA may constrain the Legislature from any legislation that directly or indirectly permits or regulates DFS, including the pending bill regarding the Lottery's entry into fantasy sports.

The following is a discussion of legal issues involved in the application of PASPA to state action. (PASPA is currently the subject of a challenge by the state of New Jersey pending in the Third Circuit Court of Appeals for an *en banc* review. Because of its pending status we do not discuss it here.²¹ But its outcome, whenever that is, will likely further inform the Legislature's action on these issues.)

The most relevant section of PASPA with potential application to DFS states:

It shall be unlawful for-

- (1) A governmental entity to sponsor, operate, advertise, promote, license, or authorize by law or compact or
- (2) a person to sponsor, operate, advertise, or promote, pursuant to the law or compact of a governmental entity,

a lottery, sweepstakes, or other betting, gambling, or wagering scheme based, directly or indirectly (through the use of geographical references or otherwise), **on one or more competitive games in which amateur or professional athletes participate, or are intended to participate, or on one or more performances of such athletes in such games.**

28 U.S.C. § 3702 (emphasis added).

Commission agrees that substantial "connective tissue" exists between what indisputably is viewed as "gambling" and DFS. This is an additional reason for the Legislature's attention to the DFS issue.

²¹ A limited discussion of the New Jersey – PASPA matter is included in Appendix A

Before PASPA can be applied to DFS it must be determined that DFS constitutes a “lottery, sweepstakes or other betting, gambling or wagering scheme based, directly or indirectly on ... one or more performances of such athletes in such games.” Thus, the first question to answer is whether DFS qualifies as a lottery, sweepstakes, betting, gambling or wagering scheme. Without getting into the details of the federal cases that have addressed what comprises such “schemes,” the Commission believes that for reasons detailed in Appendix B, that DFS would be subject, as a threshold matter, to PASPA.

1. Is DFS “Based on” Athletic Contests or the Performances of Athletes in Such Contests?

After determining that DFS contests qualify as a “betting scheme,” a reviewing court would next need to examine if they are “directly or indirectly” based on “one or more competitive games in which amateur or professional athletes compete, or are intended to participate, or on one or more performances of such athletes in such games.” While DFS contests are not based on the actual results of any specific games, they are based on the performances of athletes. Specifically, the success of the individual athletes that make up a participant’s team, when filtered through the scoring rubric set up by the DFS operator, will result in the win or loss of the participant. While a participant is not betting that a specific player achieve a particular milestone, such as scoring three touchdowns, that participant is betting that the aggregate performances of the individual athletes on his team will exceed the aggregate performance of the individual athletes on his opponents’ teams. Simply stated, if there were no underlying athletic performances, there would be no DFS, thus the Commission believes a DFS contest would likely be found to be “based on” those performances.

2. Potential Limits on State Action Involving DFS

In the event that DFS is found to constitute a PASPA defined “scheme,” “based on” athletic performances the analysis would next turn to the limits on state action concerning DFS. In relation to such a “scheme” under PASPA, a state cannot:

- sponsor
- operate
- advertise
- promote
- license, or
- authorize by law or compact

Critically, PASPA does not define these six verbs, which necessarily results in ambiguity in any statutory analysis, particularly with respect to the terms “promote” and “authorize.” Actions which would constitute the other four verbs are more straightforward. The fact that PASPA prohibits a governmental entity “to sponsor, operate, advertise, promote, license or authorize **by law or compact**” may suggest that conflict would only arise when a state passes legislation or joins a compact that involves one of the six PASPA verbs.

Regulation (as distinct from legislative passage of a law) that does not involve affirmative 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 mention DFS, it runs less chance of any outright PASPA challenge.²²

²² The framework for such potential legislation is addressed in detail in the final section of this White Paper.

Under PASPA there are a limited number of entities that have an enforcement right, namely, a United States Attorney General, a professional sports organization or an amateur sports organization. Given the business relationships between many of the professional sports leagues and the DFS operators, it is extremely unlikely that any PASPA challenge would be asserted from that group. Similarly, given the relationships between the professional and amateur sports organizations²³, this position may trickle down and eliminate challenges from amateur groups. With respect to the United States Attorney General, both Kansas and Maryland have existing state laws legalizing fantasy sports, yet neither has been the subject of a PASPA challenge, thus begging the question if state action addressing DFS (directly or indirectly) will actually lead to any further legal challenges.

While there appears to be little appetite for further PASPA challenges by those provided with a right of action under the statute, the lack of significant court interpretation of the statute, the inherent vagueness of the statutory terms and the pending *en banc* review in the Third Circuit of New Jersey's most recent attempt to legalize sports betting, suggests a cautious approach to state action addressing DFS directly.

There is, however, an alternative approach for the Legislature to consider. Rather than trying to anticipate unfavorable outcomes, or trying to design Massachusetts public policy that accommodates a peculiar and vague federal statute, the Legislature might simply write legislation and regulations it believes appropriate for the people of Massachusetts, and let the other actors react as they see fit. Ultimately, clarification of federal law on this (and many other) aspects of gaming law will be required; clear and decisive state action may further that objective.

²³ An "amateur sports organization" under PASPA is defined in relevant part as "(A) a person or governmental entity that sponsors, organizes, schedules or conducts a competitive game in which one or more amateur athletes participate or (B) a league or association of persons or governmental entities described in subparagraph (A)." Notably, the interests of the amateur sports organizations and the professional leagues are not always aligned as demonstrated by the NCAA's request that DFS operators stop offering contests based on their college sports, thus leaving the NCAA as a potential wild card PASPA plaintiff.

C. Unlawful Internet Gaming Enforcement Act (UIGEA)

UIGEA is another federal statute that has been widely cited in conversations addressing the legality of DFS. It contains a carve out in the definition of “bet or wager” that exempts fantasy sports. UIGEA 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.” The focus of the statute was the exploding online poker industry and its passage effectively eliminated online poker in the U.S. It is essentially an enforcement act dealing specifically with payment processing.

However, UIGEA also contains a critical “Rule of Construction” that explains: “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.” (emphasis added). This fact is conveniently ignored by DFS operators who frequently rely on the UIGEA carve-out as the basis for the purported legality of the games. Thus, UIGEA defers to any other federal or state law that prohibits or regulates gambling, including DFS. Despite the fact that UIGEA did not expressly legalize DFS and deferred to applicable state and federal law concerning gambling matters, some states have looked at its carve out language as a road map for state legislation. The Commission believes that such an approach is flawed and would likely result in significant problems with statutory interpretation. Since the Commission believes state law will supersede UIGEA, we do not discuss it further here. However, a more detailed analysis of UIGEA is found in Appendix C.

III. ISSUES REQUIRING REGULATION

Notwithstanding Massachusetts' unsettled legal territory with respect to DFS and the potential limitations on state regulatory actions presented by PASPA, any suggestion to regulate DFS in Massachusetts benefits from an analysis of both the rationale for regulation, and the specific issues to regulate. This section will address some of the fundamental questions pertaining to the need for regulation, identify the critical public policy issues posed by DFS, and suggest the relative merits of possible approaches. Specific suggestions regarding the framework of a regulatory approach will appear later in this Paper.

A. Rationale for Regulation

The Gaming Commission believes that the issue of “whether to regulate DFS” is largely settled.

After several years of a largely laissez-faire environment, there is a growing consensus amongst regulators, industry analysts and the DFS industry itself that some form of regulation is necessary not only to protect the interest of DFS players, but also to provide some clear guidelines and predictability to DFS operators. The confluence of the media “blitzkrieg” waged by the two DFS industry leaders this summer and the insider information concerns widely reported in October 2015 cast the industry in a new light in the public's eye, and provided a precipitating event for a broad discourse on issues that had been heretofore under-examined. Concerns regarding the potential for fraud and collusion, questions surrounding the fairness of the competitions, and a lack of clear consumer protections all pointed to the need for some effort – whether regulatory or otherwise – to provide the general public with the assurance that they could trust the industry and the integrity of the competitions. While there is an ongoing effort by the Fantasy Sports Trade Association (FSTA) to implement a regime of self-regulation, the momentum on the issue has shifted significantly to a perspective recognizing the necessity for government regulation, exemplified by FanDuel CEO Nigel Eccles' stated position that “now is the time to memorialize them [regulations] in law”. While cautious of the potential breadth of regulations, and fearful of a patchwork implementation across the country, the other major DFS operators have all publicly recognized the need for government regulation to provide security to customers and operators alike. The majority of the debate in this area continues to focus on the form and extent of a future potential regulatory environment.

In the past, legislators and regulators typically approached the issue of gaming legality by asking the question, “is it gambling?” and often “is it a game of skill or a game of chance?” As discussed above, much of this analysis has been a residue of moral judgements initially asserted hundreds of years ago, and carried forward in many religious and ethical constructs, and the definitions of “gambling,” “skill” and “chance” have often been unclear at best. Even with these religious and ethical disapprovals, however, gambling of one sort or another—especially lotteries—has been approved and utilized by government jurisdictions and other institutions as a means of raising revenues and providing entertainment since at least the beginning of this Republic.²⁴ And much more recently, the Legislature and the people of Massachusetts have emphatically endorsed many forms of gambling by way of the legalization of the Lottery and casinos.

We are left now with a public policy position that seems to assert that gambling is bad/illegal, except when it is not. And what makes gambling not bad/illegal is when the Legislature authorizes a regulatory framework and a public purpose for a particular kind of gambling. Generally speaking, we have largely come to accept gambling as a legitimate form of economic activity, entertainment and public or philanthropic revenue generation (even within the religious community) – under certain regulatory conditions.

Perhaps, as a consequence of profound changes in public values and public policy, the challenge for the Legislature about DFS and other Internet-based gaming, is to define gambling clearly and carefully. For example, the Legislature might use this definition: “Is this economic activity characterized by a payment by a player for an opportunity to win an award based on the outcome of a future event, which is not otherwise regulated?”

The Commonwealth routinely regulates most economic activity, at some level of intensity, looking into the nature of that activity to determine whether and how to regulate. In this case, it may be helpful to define in law the specific features that might be considered gambling, to serve as the tripwire for a greater than normal degree of regulation. If the proposed economic activity has these defining features, it will be considered gambling, and then the checkered history of gambling, the

²⁴ The Gaming Commission has a copy of a “Massachusetts Lottery” ticket from May 1758, the owner of which “shall be entitled to any prize drawn against said Number, in a LOTTERY granted by an Act of the General Court of the Province before said, in April 1758, towards supplying the Treasury with a Sum of Money for the intended Expedition against Canada, Subject to no Deduction.”

continuing public ambivalence about gambling activities, and long established public policy, suggest a number of key topic areas that may require regulatory consideration.

B. Identifying Issues that Require Regulatory Consideration

Acting on the invitation of the Legislature and the Governor, the Massachusetts Gaming Commission (MGC) has attempted to help advance the Commonwealth's understanding of the public policy issues surrounding DFS. The MGC's efforts were conducted in conjunction with the Massachusetts Attorney General's Office, as Attorney General Healey promulgated first-of-their-kind consumer protection regulations regarding DFS. The MGC has leveraged its growing regulatory experience and expertise to provide an independent perspective on the issues. In addition, the MGC convened industry representatives and experts to discuss the state of the industry, identify public policy issues, and consider possible remedies to these issues. The MGC's fact-finding culminated in a public Educational Forum on DFS, which included representatives from DraftKings and FanDuel – the two largest DFS operators – along with industry thought leaders, regulators (including representatives of the Attorney General's Office), and experts on technical standards in online gaming. The discussion below presents a distilled understanding of the public policy issues presented by DFS as identified throughout this process. It is worth noting that this list closely mirrors the issues addressed in the Attorney General's proposed regulations as well as a number of other emerging frameworks, including the National Council on Problem Gambling Fantasy Sports Consumer Protection Guidelines (issued in conjunction with a DFS operator, DraftDay). This indicates that just as regulators, industry experts and DFS operators have moved toward a consensus regarding the *need* for regulation, so too has a consensus begun to coalesce around the issues that need to be addressed.

The following issues and potential remedies are presented as a starting point for consideration when evaluating the appropriate regulatory schema. To simplify analysis, these issues are presented in the table below across five, broad policy areas:

Know your Customer: Ensuring that players are of legal age and are playing in a jurisdiction where DFS play is allowed. Ensuring that DFS operators can uniquely and accurately identify each and every DFS player.

DFS Player Protection: Ensuring that players' funds are properly protected, and that players understand the nature of the games, the risks involved and have access to tools and resources if they feel they have a problem.

Technical Security: Ensuring that the wealth of personal information regarding players is protected, the system cannot be manipulated to any player's advantage, and all user activity data is retained for auditing and research purposes.

Suitability and Licensure: Ensuring that regulators know the principals involved in DFS operations, and that there is a level of investment that increases the costs of non-compliance.

Impact on Real-World Sports: Ensuring that the relationship between DFS and the sports for which it provides contests does not adversely affect the perception (or reality) of fair play.

Please note that as stated in the table, the "Potential Risks" are not a statement of fact, but rather statement of risk that could exist. In discussion with the industry, the MGC has learned that many of these issues are being addressed, or have already been addressed. However, until such time as this is challenged or verified by a regulator or other governmental authority, these remain – for the sake of discussion – open issues.

DFS Issues of Concern

Policy Area	Issue	Potential Risk	Potential Remedy
"Know Your Customer"	Age Verification	• Underage players participate	• Ensure use of verified technology solutions (including 3rd party verifiers)
	Identity Verification	• Operators cannot accurately and uniquely identify players • Operators cannot limit users' ability to create multiple accounts • Operators cannot track unique users' gaming activity on site	• Ensure use of verified technology solutions (including 3rd party verifiers)
	Location Verification	• Players from restricted or excluded jurisdictions participate	• Ensure use of verified technology solutions (including 3rd party verifiers)
DFS Player Protection	Funds Protection	• Player deposits not protected • Player "bonus" funds are not protected • Unauthorized funds withdrawals • Commingling of operational and player-deposited funds • Players unable to access deposited funds upon demand	• Require monitoring to ensure segregation of deposited/operational funds • Require outside financial guarantees in case of failure
	Transparency	• Playing field not level due to unfair information disparities (insider information) • Playing field not level due to selective use of software tools "scripts" to automate tasks • Winners not transparent • Odds are not clear	• Prohibit play by individuals with access to insider information • Ensure that tools are equally available to all players • Require clear identification of winners • Require 3rd party validation of information

Policy Area	Issue	Potential Risk	Potential Remedy
		• Player pools not constructed fairly (i.e. “Sharks” vs. “Minnows”)	presented to players • Require clear/comprehensible disclosure of odds (where possible) • Limit number of entries • Require release of raw, anonymous player data (no Personally Identifying Information) for 3rd party aggregation and analysis • Limit ability to enter certain contests based on past performance (i.e. tiered contests based on past success)
	Responsible Gaming	• Players cannot control their play • Players lose money and chase losses • Players do not perceive DFS as “gambling”	• Require clear/comprehensible disclosure of odds (where possible) • Require information on game rules and expected payouts for contests • Require ability to self-exclude • Require informed choice options • Require ability to set limits on play • Require staff training on spotting and addressing problem gaming • Require reference to problem gaming resources
Technical Security	Network Security	• User data not protected • Contests artificially manipulated	• Enforce existing data security laws • Require regular information security audits

Policy Area	Issue	Potential Risk	Potential Remedy
			• Require 3rd party penetration testing
	Forensic Accounting/Anti-Money Laundering	• Operators cannot account for individual users' activity to check for suspicious/illegal behavior including money laundering	• Require retention of user activity audit data • Leverage existing work of payment processors
Suitability and Licensure	Operator Suitability	• Principals involved in DFS operations are largely unknown to regulators • Lack of investment in license fee and absence of suitability investigation increases risk of non-compliance by operator	• Create licensing schema to include DFS Operators • Create definition of "suitability"
Impact on Real-World Sports	Insider Information – Team	• Playing field not level due to unfair information disparities (insider information)	• Require DFS operators to exclude play by employees and athletes of participating sports teams.
	Insider Information – DFS Companies	• Playing field not level due to unfair information disparities (insider information)	• Require DFS operators to exclude play by employees.
	Game and Athlete Integrity	• Game and athlete integrity is questioned if athletes allowed to participate in DFS contests	• Prohibit athletes and league personnel from playing

Another way for the Legislature to consider issues that might require regulatory attention is to draw on its past experience in establishing regulatory parameters for other gaming initiatives in the Commonwealth – casinos, Lottery, and horse racing. Although they are all organized somewhat differently, the following list of regulatory principles embedded in current statutes and the Attorney General’s proposed regulations are quite similar in scope to those enumerated in the chart above.

**REGULATORY PRINCIPLES EMBEDDED
IN CURRENT STATUTES (Chapters/Section) & REGULATIONS**

1. Oversight by regulatory body

- a. Lottery: Ch. 10/§23, §24
- b. Racing: Ch. 128A/§9
- c. Casino: Ch. 23K/§3, §69, §70

2. Consumer protection

- a. Broad gov't authority over games, payouts and accounting
 - i. Lottery: Ch. 10/§24
 - ii. Racing: Ch. 128A/§5, §5C, §9; §128C
 - iii. Casino: Ch. 23K/§4, §5, §35, §36
- b. Disclosure of odds
 - i. Lottery: Ch. 10/§24A
- c. Minimum age
 - i. Lottery: Ch. 10/§29
 - ii. Racing: Ch. 128A/§10
 - iii. DFS: 940 CMR 34.04, 06 (Proposed)
 - iv. Casino: Ch. 23K/§25, §54
- d. Security of deposits
 - i. DFS: 940 CMR 34.05 (Proposed)
- e. Content of Advertising
 - i. DFS: 940 CMR 34.07, 09 (Proposed)
- f. Use of non-public information
 - i. DFS: 940 CMR 34.12 (Proposed)
- g. Grouping by skill level
 - i. DFS: 940 CMR 34.06, 12 (Proposed)
- h. Assuring integrity of gaming devices
 - i. Casino: Ch. 23K/§66

3. Prevention of criminal or other undesirable conduct

- a. Licensing & registration
 - i. Lottery: Ch. 10/§27
 - ii. Racing: Ch. 128A/§2, §3, §11, §11C
 - iii. Casino: Ch. 23K/§9, §12-16, §30-33
- b. Focus on Organized crime
 - i. Lottery: Ch. 10/§24
- c. Power to exclude patrons and others
 - i. Racing: Ch. 128A/§10A
- d. Law enforcement powers
 - i. Casino: Ch. 23K/§6, §35, §37-44
- e. Prohibited campaign contributions
 - i. Casino: Ch. 23K/§46, §47
- f. Research consequences
 - i. Casino: Ch. 23K/§58, §71

4. Revenue generation for dedicated purposes

- a. Cities and towns
 - i. Lottery: Ch. 10/§25, §35
 - ii. Racing: Ch. 128A/§5
- b. Other specified beneficiaries
 - i. Lottery: Ch. 10/§57
 - ii. Racing: Ch. 128A/§5
 - iii. Casino: Ch. 23K/§53-64
- c. Ensuring integrity of revenue stream
 - i. Casino: Ch. 23K/§25, §65

5. Mitigation

- a. Adverse Community impacts
 - i. Casino: Ch. 23K/§17, §18
- b. Problem gambling prevention
 - i. Lottery: Ch. 10/§24A
 - ii. DFS: 940 CMR 34.10, 11 (Proposed)
 - iii. Casino: Ch. 23K/§26, §27, §28, §45
- c. Horse health support (Tufts): Ch. 128A/§5
- d. Child support
 - i. Lottery: Ch. 10/§28A
 - ii. Casino: Ch. 23K/§51, §52
- e. Prevention of cannibalization
 - i. Lottery: Ch. 10/§27
 - ii. Casino: Ch. 23K/§18

6. Job creation/economic development

- a. Lottery: Ch. 10/§27
- b. Racing: Ch. 128A/§5
- c. Casino: Ch. 23K/§10, §11, §18

7. Self sustaining regulatory body

- a. Lottery: Ch. 10/§25
- b. Racing: Ch. 128A/§5B
- c. Casino: Ch. 23K/§56

IV. CONSIDERING A REGULATORY MODEL

Once the Legislature has determined whether and how the issues identified above need regulatory attention, it will need to turn to the question of what form of regulation is appropriate.

Regardless of the exact regulatory approach adopted, the intent of any form of regulation should be to remedy either the potential dangers to consumers or the negative externalities of the industry, not to artificially or needlessly constrain the industry. An effective regulatory schema (like the draft regulations proposed by the Massachusetts Attorney General) should provide measured “tools” for regulators to use to either (1) promote a public good, or (2) mitigate a potential risk. As such, any analysis of a proposed regulatory approach must begin with an understanding of the issues and risks at hand; next consider potential tools to address these issues; and finally weigh options for how to effectuate those regulatory tools in such a manner that clearly connects the public interest being served with the burden being imposed.²⁵ Finally, in this particular case, given the nascent nature of the DFS industry and its likely, but unpredictable evolution, the issues examined should be fundamental in nature (broadly defined) so as not to confine the analysis to the games as they currently exist, but rather to identify and anticipate the universal public policy issues of concern both now and in the future.

There are multiple regulatory models that could be employed to address the issues outlined above. The Attorney General’s proposed regulations consider most of the important issues of concern and provide consumers with a powerful tool to address their concerns and grievances. This tool, however, necessitates that an aggrieved consumer or law enforcement agency seek remedy which for many may be too costly or time consuming to pursue, and which in any case provides only a very random and reactive method of enforcement. An appropriately robust regulatory structure should consider how to work in concert with the Attorney General’s proposed consumer protection regulations to address these same concerns prospectively, so that issues are detected and addressed, or avoided altogether without the need for consumer action.

²⁵ This is a sentiment that was echoed several times throughout the December 10, 2015 DFS Educational Forum, best summarized by Kevin Mullally, Vice President of Government Relations and General Counsel for Gaming Laboratories International, LLC who said, “I firmly believe that when you start looking at an activity that you deem worthy of regulation that for every requirement you should have a specific public policy objective. You should be able to very distinctly and specifically ...identify what risk you’re trying to mitigate or what public benefit you are trying to advance and make it proportional to the risk.”

Such a model would require a body or an agency to promulgate regulations, monitor compliance, enforce corrective action and continuously work with the DFS operators to ensure the proper functioning – from a regulatory perspective – of the industry. Still, given this goal, there remains a spectrum of possible approaches, ranging from the “heavy” regulatory environment imposed upon the brick-and-mortar casino industry, to a “light” regulatory schema that accepts increased levels of risk and limits both the requirements placed on industry and the resultant compliance monitoring.

A “heavy” casino-style approach should be examined, but any examination should be mindful of the potential financial burden on an industry that has yet to prove profitable over time. Additionally, consideration should be given to the fact that brick-and-mortar casino regulations originated in an environment replete with criminal involvement and subsequently developed over time to address risks that were repeatedly disclosed. This template for traditional casino regulation is now well established and provides less flexibility to regulatory bodies, as the risks are well documented and the approaches largely harmonized across jurisdictions.

DFS is a virtual business in nature and has a small-to-nonexistent physical footprint in a given jurisdiction. This consideration, along with the fact that DFS outsources much of its risk dealing with money and customers to third party payment processors, eliminates some of the concerns surrounding traditional casinos. A “light” regulatory schema with more discretion afforded to the regulatory body to make judgement calls might make sense in that it may provide the necessary flexibility to address both evolving technology and evolving issues given the contemplative pace of legislative change. Additionally, given the data-driven nature of DFS, there are opportunities to employ hands-off, big-data style approaches to regulation analogous to Central Monitoring Systems used to monitor slot machine activity in traditional casinos. Such systems offer comprehensive oversight with little to no hands-on or physical regulation.

In considering the appropriate kind of regulatory scheme for DFS and other on-line gaming, certain principles are worth bearing in mind:

- The scheme must be commercially viable
- The scheme must be technologically feasible
- The scheme should attempt to balance the “problem solved” with the “cost increased”
- The scheme should be “risk-based,” balancing the risk and seriousness of the problem with the cost and imposition of the solution

Whatever the outcome, careful thought should be afforded to the design of the regulatory approach, as many other jurisdictions may look to the first successful model for guidance, and the DFS industry’s desire for a consistent regulatory approach will remove barriers to implementing a “smart” model. Further discussion of this proposal is found in Section VI: An Omnibus Regulatory Approach to Internet Gaming.

V. THE PROFILARATION OF INTERNET GAMING

The discussion thus far has focused primarily on DFS and the considerations surrounding the availability of that form of Internet activity in the Commonwealth. This focus is appropriate because the rapid expansion of DFS and the uncertain legal environment in which it operates demand immediate and careful consideration. At the same time, however, DFS is only one form of Internet gaming activity that the Commonwealth is likely to encounter in both the near and long term.

Internet gaming opportunities are abundant today and will almost certainly grow quickly. Those opportunities were discussed at length in an October 26, 2015, memorandum entitled “Internet Gambling” that is posted on the Commission’s website at <http://massgaming.com/wp-content/uploads/Internet-Gaming-Memorandum-10-26-15.pdf>. In summary, although only Delaware, New Jersey and Nevada currently permit Internet gambling, Internet gambling here and abroad, legal and illegal, is a huge enterprise. As reported in a recently completed study commissioned by the American Gaming Association, an enormous amount of illegal Internet gambling opportunities are available in the United States. Indeed, their widespread availability, the risk to bettors they pose and the loss of tax revenue they create have been used as arguments for permitting state created and controlled Internet gambling opportunities in the United States and elsewhere. Outside of the United States, including Europe, there is an enormous amount of legal and highly regulated Internet gambling activity.

Internet gaming or gaming-like economic activity falls into one or more of six broad categories.

A. Casino Games

At present, three states currently allow casino-type Internet gaming. New Jersey and Delaware, two of the three states where Internet gambling is permitted, allow participants to play virtual slot machines as well as virtual table games including craps, poker and blackjack. Participants must be physically located within the New Jersey or Delaware borders and their presence within those boundaries is assured by sophisticated software. Age limits also apply. Both states use age verification protocols in which they have a high degree of confidence, though it is always possible for a participant of the proper age to allow an underage person to play Internet games using the participant’s name and bank account. Gaming activity in both states is principally governed by state

law and regulations, though some federal law is applicable and is described in the memorandum mentioned above.

Nevada, the third state where Internet gambling is allowed, only permits Internet poker. Nevada has entered a compact with Delaware so that Nevada players can play poker at Delaware sites and vice versa. Again, Nevada players must be physically located in Nevada in order to play and Nevada uses age verification protocols for all participants

In addition to those three states, ten others – Pennsylvania, Alabama, Iowa, California, Connecticut, Illinois, New York, Pennsylvania, Rhode Island, Texas and Washington – have considered authorizing Internet play. Thus far, none has done so. In the spring of this year, it appeared that Pennsylvania would very likely have Internet gaming before the end of the year but the legislative session expired before any of the pending measures were enacted and a renewed discussion late in the year likewise failed to produce authorizing legislation. Illinois is in the middle of a very serious budget crunch and that may cause legislators to push forward with thus far unsuccessful efforts.

Here in Massachusetts, two Internet gaming bills were filed last session but neither made it out of committee. This year, three bills are pending, two of which deal with the Lottery. The first, S151, was introduced by Sen. Flanagan and referred to the Joint Committee on Consumer Protection and Licensure. That bill would authorize the Lottery to offer online “lottery” games and would allow the Lottery to decide what those games look like. Last term a similar bill died in committee. A hearing on S151 was scheduled for September 15 but the Bill has not yet been reported out of Committee. The second of the two is S191, which was introduced by Sen. Rush and also referred to the Joint Committee on Consumer Protection and Professional Licensure. That bill would authorize and direct the Lottery “to implement online games of skill, including, but not limited to, fantasy sports, so-called, poker, so-called, and other games of skill, subject to the provisions of, and preempted and superseded by, any applicable federal law.” That bill has not been reported out of Committee.

The final bill is S241. Introduced by Sen. Tarr, that bill would authorize any Massachusetts Category One or Two gaming licensee to conduct gaming operations on the Internet under rules and regulations the Gaming Commission promulgates provided that “such operations do not include or reflect gaming mechanisms operated by the state lottery program o[r] those simulating or resembling slot machines.” The bill was referred to the Joint Committee on Economic Development

and Emerging Technologies. The Committee held a hearing on the bill on November 10, 2015 but the bill has not been reported out.

B. Sports Betting

A second well-established form of Internet gambling involves betting on sports. Primarily four sports -- horse racing, professional sports, fantasy sports and, now, eSports – are involved. While a wide variety of sports betting is available outside the United States, most sports betting is illegal here. Nevertheless, illegal sports betting in the United States involves hundreds of millions of dollars, a fact that underlies at least some of the pressure to legalize and regulate all of the betting activity.

Of the four, horse racing is probably the most well-entrenched. Federal law permits state regulated horse racing and interstate off-track betting. As a result, betting is available on a number of Internet sites. Bettors can wager on races at hundreds of tracks throughout the world on desktop and mobile devices as well as at off-track betting sites. On the Internet, the bettor makes a deposit at the site, virtually goes to the track of his or her choice and places a bet out of the amount he or she has on deposit. If the bettor picks a winner, the winnings are deposited into the bettor's account. All sites contain some handicapping information but stand-alone programs also provide handicapping information, some for free and, in much more detail, some by paid subscription.

Betting on professional and collegiate sports is prohibited by federal law except in Nevada, Delaware, Montana and Oregon, which were exempted from the federal ban because they permitted sports betting when PASPA was enacted. Nevada permits sports betting through licensed bookmakers at physical locations and online, Delaware permits a "parlay" form of sports betting and the other two states do not permit any betting on any sport. Several years ago, New Jersey enacted legislation designed to allow sports betting in a manner that legislators believed was consistent with what they saw as the terms of the federal ban. Major league baseball, football and hockey along with the NCAA challenged the New Jersey legislation in federal court and the suit is now before the United States Court of Appeals for the Third Circuit sitting *en banc*. A New Jersey victory in the suit would likely provide a foundation for other states to undertake a similar approach, one that might well include intrastate betting via the Internet.

Fantasy sports is the newest, hottest and now most controversial offering in the sports betting area and has been explored thoroughly in earlier portions of this Paper.

C. eSports

The Wikipedia description of eSports accurately and succinctly describes eSports as “organized multiplayer video game competitions, particularly between professional players. The most common video game genres associated with electronic sports are real-time strategy, fighting, first-person shooter, and multiplayer online battle arena. Tournaments . . . provide both live broadcasts of the competition, and cash prizes to competitors.”

At present, eSports competitions are viewed over the Internet and at live performances in large capacity auditoriums. One of the largest Internet eSports sites announced last June that it was broadcasting an average of 1.5 million games per month to an average worldwide audience of 100 million monthly viewers. Indeed, Sports Illustrated recently reported that in 2014, 27 million worldwide fans watched an eSports world championship match between teams from South Korea and China. That audience was more than the 23.5 million who watched the clinching games of last year’s World Series or the 17.9 million who watched the final game of the NBA playoffs. Recognizing the size of the audience and the popularity of the games, Turner Broadcasting Company recently announced that it plans to run two 10 week tournaments in 2016 with a live broadcast of a contest on TBS stations throughout the country each Friday night during those 10 week periods.

D. Social Gaming

Running parallel to real money gambling is a form of entertainment known as social gaming. That label stems from the fact that Facebook has historically been the gateway to many of the most popular games. Today, however, the label now applies to all forms of Internet gaming in which prizes remain in the game and cannot be redeemed either for real money or for other tangible rewards.

Some of the games bear no resemblance to casino games. Nevertheless, games that resemble casino games today proliferate. Virtually all of the games, casino and other, use the “freemium” model in which new players receive an initial amount of play money for free and can purchase more when

that supply is exhausted. The vast majority of the games do not offer any tangible rewards for successful play or any ability to convert the play money into real money or other things of value. Some, however, link success on the social gaming site to some form of recognition, tangible or otherwise, when the player visits a brick-and-mortar casino facility with which the social site is affiliated. Currently, social gaming is a big business. Some estimates suggest that worldwide social gaming revenues will approach \$30 billion in 2015, though that includes all forms of social games, not just those that resemble games available in casinos.

E. Skill Based Games

In addition to the games just described, some sites offer what appear to be true games of skill in which one can play against an opponent for real money. Games of skill are those in which dexterity, problem-solving ability or other player attributes have a far greater role than chance in determining the outcome of the game. One company, for example, offers very realistic bowling and darts games that a participant can play on a mobile device either alone for free or in competition for real money with another player. Nevertheless, each contains some elements that may not be visible to the player. In the bowling game, for example, elements of chance such as pin placement, the algorithm that determines which pins fall when the ball strikes, the skill of the opponent, the role played by the "oil" on the lane or other game elements likely affect at least some part of the play.

Currently, casino operators and slot machine manufacturers are exploring the extent to which skill based games should replace at least some of the more familiar slot machines on casino floors. Nevada will likely set the standard for the new games and machines, at least for the immediate future and has already drafted regulations on the subject. (And in Massachusetts, the Gaming Commission is considering regulations that would make skill based slot machines acceptable in Massachusetts casinos.) It will be important to watch Nevada developments because some, and perhaps most, of those games can migrate easily to the Internet or already exist on the Internet as social games and can migrate to the gaming floor.

F. Prediction markets

Prediction markets are another area of Internet activity that involves investment and return based on the outcome of a future event. Essentially, prediction markets contain a series of questions, typically though not exclusively questions that can be answered "yes" or "no," that have been prepared by the market sponsor or host. The market allows individuals to buy "shares" of a "yes" or "no" answer to those questions. All shares have an ultimate value of \$1.00. Individuals buy "yes" or "no" shares based on their assessment of the likelihood that the event will or will not occur. The market matches purchasers of "yes" shares with purchasers of "no" shares and vice versa. The market determines the price of the shares based on its collective judgment about the likelihood of the event's occurrence. For example if the question were "will Candidate X win the upcoming gubernatorial election" and the market concluded that it was just as likely that Candidate X would win as it was the he or she would lose, the price for both "yes" and "no" shares would be \$.50. If the market determined that Candidate X only had a 30% chance of winning the election, then "yes" shares would cost \$.30, "no" shares would cost \$.70. After the event, be it the election or some other event occurs, the shareholder who holds shares matching the actual outcome collects \$1.00 (typically minus a 10% transaction cost taken by the operator) and the person who holds the non-matching shares collects nothing. The market also permits shareholders to sell their shares as the market price for them changes, thus allowing a shareholder to cut losses or preserve gains before the event occurs.

At present, two companies host prediction markets of the type just described. The first is called Predictit, and is run by the University of Wellington in New Zealand assisted by a company called Aristotle International, Inc., a well-known Washington DC provider of technological and other assistance to political and public affairs campaigns. At the Predictit site, \$850 is the maximum amount an individual is permitted to invest in the shares of any single question. The other site is called IEM, which is an acronym Iowa Electronic Market, and is hosted by the University of Iowa. There, \$500 is the maximum amount an individual is permitted to have in his or her investment account at any one time. Both Predictit and IEM have received "no action" letters from the Commodities Futures Trading Commission and are otherwise unregulated. A third site, called Predictwise, does not allow monetary investments but instead aggregates answers to questions in real time and displays the aggregate answer in constantly updated graphics.

VI. AN OMNIBUS REGULATORY APPROACH TO INTERNET GAMING

Internet gaming (also referred to as “online” or “remote” gaming) offers a dizzying and constantly expanding variety of games. Any new regulatory effort for just one of these games will surely beg the question of how to handle the others. A regulatory strategy that is broad enough and flexible enough to adapt to any and all of these proliferating games may be worth serious consideration.

All of the Internet activity just described as well as activity that is sure to come shares common characteristics. The activities are innovative and rapidly deployed. When combined, innovation and speedy deployment make it difficult to determine quickly whether and to what extent the activities pose risks to the public and to decide who is responsible for making that determination. If policymakers decide that an activity does pose risks, it can be difficult to determine whether the risks are of sufficient magnitude to require a new legislative framework or whether new regulations or other oversight by an existing regulatory body suffices. Because the activities can be and frequently are modified quickly, whatever decisions are made at the outset about the need for regulation may require frequent revisiting. Given the dynamic nature of the Internet, the public appetite for Internet games and gaming, the creative energies and talents of game creators, and the low barriers to entry of new games and approaches to gaming, those difficulties are likely to accelerate in the years ahead.

As recent history and litigation demonstrate, it is not enough – indeed, it is frequently not fruitful – simply to ask whether a new form of Internet activity involving payment of money for future rewards constitutes “gambling”. Given the complexity of the Commonwealth’s gambling statutes, the answer to that question in any given case may not be clear, as we have discussed at length in an earlier portion of this Paper. While an activity that combines price, prize and chance often looks like gambling, Massachusetts law is not always clear on which gambling-like activities are legal and which are not. As previously discussed, “chance” and the role chance plays in determining a given outcome can vary widely from activity to activity. Moreover, the answer to the “is it gambling” question does not necessarily determine whether it is good public policy to prohibit the activity nor does it determine the nature and kind of regulation appropriate for the activity if it is permitted.

The real question, then, is how to determine whether a new Internet activity involving payment of money in return for future rewards ought to be regulated and, if so, how and by whom. Not all such

activity necessarily requires regulation. Even when regulation is required, regulations and the regulatory framework must be of the right size, i.e., neither so onerous that it stifles positive economic activity nor so lax that it fails to protect the public interest.

Basically there are three legislative approaches to determining the nature and type of appropriate regulation and the identity of the appropriate regulators:

A. The “Chapter 23K” Approach

First, the Legislature could examine each new activity or category of activity, decide whether and to what extent it should be regulated and, if new regulations are required, create a legislative framework within which that regulation will occur as it did with casino gambling in Chapter 23K. The difficulty with this approach stems from the inherent nature of the legislative process, a process that is deliberative, careful, consensus-based and thoroughly debated - such as the process that produced the expanded gaming legislation. Those characteristics give the process an enormous strength. But those characteristics may pose obstacles to a rapid response to new Internet developments that may be required to mitigate quickly the public dangers innovative Internet activity can present. Moreover, those characteristic may make it difficult to respond with appropriate speed to fundamental changes in that activity after a regulatory framework is initially deployed.

B. The “Leave It Alone” Approach

A second approach is for the Legislature simply to allow existing branches of government, including the administrative agencies they contain, to determine whether a new Internet activity involves some element or elements falling within their existing regulatory authority. This approach has the benefit of drawing on the expertise many agencies currently possess. Nevertheless, it has the drawback of requiring the agencies, perhaps at the state, regional and local levels, to decide what portions of the new activity fall within their regulatory authority and then how that authority should be exercised. Although the Attorney General’s proposed DFS regulations demonstrate that existing law can be utilized to adapt to new gaming innovations, earlier comments have suggested that consumer protection regulations alone may be inadequate to the regulatory need. And in a balkanized environment of that sort, decision-making may lag far behind the activity itself. In

addition, more than one agency—or perhaps no agency— may legitimately feel that it has at least some responsibility for regulating the activity, leading to the possibility of regulatory efforts that either work at cross purposes, even as regulators of competence and good faith seek to avoid that result, or fail altogether.

C. The Omnibus Regulatory Approach

A third approach is for the Legislature to recognize that because Internet gaming activity is unique, quickly deployed and highly malleable, regulation ought to be reposed in a single, nimble Internet gaming regulatory body. This approach would require new legislation, but the regulatory body could be one that currently exists or one that the Legislature creates. Such omnibus on-line gaming regulatory legislation would establish the Commonwealth's overriding public policy objectives and regulatory principles, presumably including the principles embodied in existing horse racing, gaming and lottery legislation, and enumerated previously in Section III. Minimally, such legislation would direct that organized crime and individuals with criminal backgrounds have no operational control over the gaming activity, that players are protected from unfair or deceptive practices when they engage in the gaming activity, that operators of the activity take appropriate steps to mitigate the adverse consequences the activity may produce, and that the activity produces economic benefits for Massachusetts. The economic benefits may come through taxation of the activity at a rate the Legislature determines but also through encouragement of Massachusetts job creation and economic development.

If such an omnibus online gaming regulatory body were created, it would be important to give it jurisdiction also over all Internet-based (or "online" or "remote") economic activity in which a person stakes or risks something of value on the outcome of a future event, whether that outcome is dependent on chance, the individual's skill or a combination of both. So formulated, the regulatory body's jurisdiction would be broad enough to invest it with the power to look at all Internet gaming activity, determine whether any form of regulation of that activity is necessary and, if it is, create "right-sized" regulations to deal with it, pursuant to the public policy objectives and regulatory principles in the Legislature-promulgated enabling legislation. With that broad mandate, the agency would inevitably keep itself abreast of developments in the Internet gaming industry and develop a body of expertise allowing it to decide quickly the kinds of dangers the new activity posed or presented and impose the measures tightly tailored to preventing those dangers.

To be sure, an agency with a broad mandate of that kind and description would have considerable power to affect what could become a broad swath of economic activity on the Internet. Accordingly, legislative oversight, even if in arrears, would be highly desirable. To that end the agency could be required to file quarterly reports, engage in periodic briefings of legislative committees or even, as in the case of horse racing regulations, be required to deliver proposed regulations to the Legislature and delay implementation for a period of time while legislators pondered their potential impact. In any event, an Internet regulatory body with that kind of a broad mandate and developed expertise would be prepared to provide the Legislature and the citizens of Massachusetts with informed regulatory measures, promptly, economically, and thoughtfully, to avoid palpable dangers while promoting economic growth in a dynamic arena.

VII. CONCLUDING THOUGHTS

There remain a couple of important issues the Legislature will likely consider as it addresses the issue of DFS and online gaming, which we refer to in the body of this Paper only tangentially. The first is taxation—the issue of whether and how to impose extraordinary taxes on one or more of these new gaming approaches. This is an issue solely for deliberation by the Legislature. The Commission notes only that legal gambling is typically subjected to extraordinary tax rates, both when there are very high profit margins (casinos) or when the gaming is barely profitable (pari-mutuel betting on horse racing); that these taxes are typically assessed on gross revenues, rather than profits; and that such gross revenue taxes can be an impediment to viability for new and innovative gaming companies.

The second issue is one-time licensing fees dedicated to a public purpose. Again, this is effectively a tax issue, in the sole discretion of the Legislature. The Commission notes only that significant license fees can serve as a way to limit participation to serious (or at least well-heeled) operators and developers; that such license fees can serve to enhance operator compliance with laws and regulations, since it gives the operator meaningful “skin-in-the-game;” and that such fees can be an impediment to viability for new and innovative gaming companies.

The Commission hopes to have made clear in this Paper that there is some urgency for the Legislature to address the issue of DFS. Unsettled Massachusetts law and piecemeal regulation make playing DFS a risky activity, both legally and practically for Massachusetts citizens, and makes operations and fund-raising highly problematic for DFS operators, including DraftKings, an innovative new economic engine in our midst. Prompt clarification of the law is highly desirable for citizens, players, and operators alike.

The Massachusetts Legislature has led the nation on a host of challenging public policy issues over the years. It has the opportunity to do so again with the challenge of DFS and the future of Internet-based gaming.

The Massachusetts Gaming Commission

APPENDIX A

NEW JERSEY LITIGATION AND PASPA

In November 2011, the voters of New Jersey approved a referendum which granted the state legislature the authority to amend the constitution to allow sports wagering. Subsequently, the legislature passed a bill allowing the state to issue licenses to the state's casinos and racetracks to permit gambling on sporting events. The bill was then signed into law. Prior to any regulations being promulgated, the NCAA, NBA, NFL, NHL and MLB filed an action in the United States District Court for the District of New Jersey to prevent the state from implementing the law asserting that it violated PASPA. The District Court found in favor of the leagues in February 2013. The state then appealed to the United State Court of Appeals for the Third Circuit to challenge the District Court's decision. In a two-to-one decision, the Third Circuit affirmed the District Court's decision. In discussing the limits of PASPA the majority explained:

Under PASPA, “[i]t shall be unlawful for ... a governmental entity to sponsor, operate, advertise, promote, *license, or authorize by law or compact*” a sports wagering scheme. 28 U.S.C. § 3702(1) (emphasis added). Nothing in these words *requires* that the states keep any law in place. All that is prohibited is the issuance of gambling “license[s]” or the affirmative “authoriz[ation] *by law*” of gambling schemes. Appellants contend that to the extent a state may choose to repeal an affirmative prohibition of sports gambling, that is the same as “authorizing” that activity, and therefore PASPA precludes repealing prohibitions on gambling just as it bars affirmatively licensing it. This argument is problematic in numerous respects. Most basically, it ignores that PASPA speaks only of “authorizing *by law*” a sports gambling scheme. We do not see how having *no law* in place governing sports wagering is the same as authorizing it by law. Second, the argument ignores that, in reality, the lack of an affirmative prohibition of an activity does not mean it is *affirmatively* authorized by law. The right to do that which is not prohibited derives not from the authority of the state but from the inherent rights of the people. Indeed, that the Legislature needed to enact the Sports Wagering Law itself belies any contention that the mere repeal of New Jersey's ban on sports gambling was sufficient to “authorize [it] by law.”

Nat'l Collegiate Athletic Ass'n v. Governor of New Jersey, 730 F.3d 208, 232 (3d Cir. 2013).

Seizing upon this rationale, New Jersey passed a law in 2014 that repealed a portion of the prior law that had criminalized sports betting at state casinos and racetracks asserting that such repeal was not an “authorization by law.”

The leagues then challenged New Jersey’s selective repeal in District Court arguing that it constituted PASPA prohibited “authorization” in disguise. The District Court judge found for the leagues and the state appealed to the Third Circuit. The reviewing panel of three judges ruled two-to-one in favor of the leagues’ argument agreeing that New Jersey’s selective repeal violated PASPA and contradicting their prior decision. The dissenting judge, Justice Fuentes, argued that it was illogical to determine that the repeal of a portion of a law was an “authorization” to do anything, either implicit or explicitly. New Jersey requested an *en banc* appeal, which was granted, the underlying opinion was vacated and the matter was scheduled for a new hearing in February 2016.

The New Jersey case exemplifies the breadth of PASPA’s application even in situations where a state arguably took no affirmative action to “sponsor, operate, advertise, promote, license or authorize” a sports betting scheme. Given the manner in which the Third Circuit interpreted the PASPA prohibition on state “authorization” of sports betting, a similar interpretation of state “promotion” of sports betting even without traditional “promotional” behavior²⁶ is equally possible. While the willingness of the Third Circuit to reconsider the New Jersey matter *en banc*, suggests an opportunity to revisit the discussion, it is impossible to predict the outcome.

The fact that PASPA prohibits a governmental 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. This same interpretation, that PASPA requires some *affirmative* state action, was discussed in the earlier of the two New Jersey cases. *Nat’l Collegiate Athletic Ass’n*, 730 F.3d at 232 (“All that is prohibited is the issuance of gambling ‘license[s]’ or the affirmative ‘authoriz[ation] *by law*’ of gambling schemes.”). There is presently a dearth of case law discussing the limits of what would constitute affirmative state action sufficient to trigger a PASPA violation; however the New Jersey case demonstrates that the selective *repeal* of legislation authorizing sports betting was enough to constitute “authorization;” thus setting the bar for a PASPA violation quite low. While this decision was vacated, it demonstrates the

²⁶ It remains unclear what is considered “promotional” state action according to PASPA.

inherent vagueness of the PASPA terms and the potential for their broad interpretation even within the same court.

Any approach to state action outside of the six PASPA verbs should be a cautious one in light of the New Jersey decision discussed at length above. 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.²⁷ Notably, the plaintiffs in the New Jersey cases were sensitive to creative draftsmanship of legislation in an effort to avoid PASPA; however, it is unclear whether those same plaintiffs would pursue a legal challenge at this time for the reasons set forth below.

Under PASPA there are a limited number of entities that have an enforcement right, namely, a United States Attorney General, a professional sports organization or an amateur sports organization. Given the business relationships between many of the professional sports leagues and the DFS operators, it is extremely unlikely that any PASPA challenge would be asserted from that group. Similarly, given the relationships between the professional and amateur sports organizations²⁸, this position may trickle down and eliminate challenges from amateur groups.

²⁷ The framework for such potential legislation is addressed in detail in the final section of this white paper.

²⁸ An “amateur sports organization” under PASPA is defined in relevant part as “(A) a person or governmental entity that sponsors, organizes, schedules or conducts a competitive game in which one or more amateur athletes participate or (B) a league or association of persons or governmental entities described in subparagraph (A).” Notably, the interests of the amateur sports organizations and the

With respect to the United States Attorney General, both Kansas and Maryland have existing state laws legalizing fantasy sports, yet neither has been the subject of a PASPA challenge, thus begging the question if state action addressing DFS (directly or indirectly) will actually lead to any further legal challenges.

While there appears to be little appetite for further PASPA challenges by those provided with a right of action under the statute, the lack of significant court interpretation of the statute, the inherent vagueness of the statutory terms and the pending *en banc* decision in the Third Circuit suggest a cautious approach to state action addressing DFS directly.

professional leagues are not always aligned as demonstrated by the NCAA's request that DFS operators stop offering contests based on their college sports, thus leaving the NCAA as a potential wild card PASPA plaintiff.

APPENDIX B

AN ANALYSIS OF DFS AS A GAMBLING SCHEME

Before PASPA can be applied to DFS it must be determined that DFS constitutes a “lottery, sweepstakes or other betting, gambling or wagering scheme based, directly or indirectly on . . . one or more performances of such athletes in such games.” Thus, the first question to answer is whether DFS qualifies as a lottery, sweepstakes, betting, gambling or wagering scheme.

A. Lotteries

The widely recognized elements of a lottery consist of the distribution of prizes according to chance in exchange for consideration. FCC v. ABC, 347 U.S. 284, 290 (1954). It is unclear what level of chance is necessary for a contest to qualify as a “lottery” under PASPA, although any such determination would be fact intensive. DFS providers would argue that their contests do not qualify as a lottery where the distribution of prizes is not by chance but dependent upon the skill of the participants and they would point to their data driven studies. Opponents would likely argue that chance is still involved in determining the winners of any DFS contests and thus they could qualify as a lottery under federal law in the absence of an established federal skill versus chance test.²⁹ Ultimately, it is likely that DFS operators would have the edge in arguing that their contests do not qualify as traditional lotteries.

B. Sweepstakes

Similarly undefined under PASPA is the term “sweepstakes.” Massachusetts law defines a sweepstakes as “any game, advertising scheme or plan, or other promotion, which, with or without payment of any consideration, a person may enter to win or become eligible to receive any prize, the determination of which is based upon chance.” M.G.L. c. 271, § 5B. At least one federal statute defines a sweep stakes as “a game of chance for which no consideration is required to enter.” 39 U.S.C. § 3001(k)(1)(D). Common dictionary definitions often conflate sweepstakes and lotteries, drawing no distinction between the two.

²⁹ For example, in Massachusetts an activity that is “predominantly” chance-based would qualify as a lottery but if it was “predominantly” skill-based it would not. There is no such corollary at the federal level.

Simply because most DFS contests require the payment of consideration to play does not eliminate DFS from potential consideration as a “sweepstakes.” As indicated in M.G.L. c. 271, § 5B, a sweepstakes can be “with or without payment of any consideration.” Similarly, many DFS contests can be played with promotional credit and result in the winning of real money prizes, thus the lack of paid consideration would not be dispositive to such an analysis. It is far more likely that any determination of whether DFS constitutes a “sweepstakes” would again turn on whether the winner was decided by chance or skill. Such an analysis would mirror that described above for lotteries.

C. Betting, Gambling or Wagering Scheme

This phrase serves as a broad catch-all within PASPA to address those “schemes” that do not qualify as lotteries or sweepstakes. Given the lack of definitions within the statute a reviewing authority would constitute common definitions of the terms. One source of such a definition is found in Massachusetts case law concerning the definition of bet as set forth in detail above. Other common dictionary definitions of “bet” find a multitude of overlapping definitions³⁰ including:

- Something that is laid, staked, or pledged typically between two parties on the outcome of a contest or a contingent issue. See <http://www.merriam-webster.com/dictionary/bet>.
- To risk a sum of money on the unknown result of an event in the hope of winning more money than you have risked. See <http://dictionary.cambridge.org/us/dictionary/english/bet>
- An agreement to risk money on the unknown result of an event. See <http://dictionary.cambridge.org/us/dictionary/english/bet>
- A pledge of a forfeit risked on some uncertain outcome; wager: See <http://dictionary.reference.com/browse/bet?s=t>.
- An act of risking a sum of money on the outcome of a future event. See http://www.oxforddictionaries.com/us/definition/american_english/bet
- A sum of money staked on the outcome of a future event: http://www.oxforddictionaries.com/us/definition/american_english/bet

³⁰ The terms “bet” and “wager” have near identical definitions even in the context of dictionary entries.

- An agreement between two parties that a sum of money or other stake will be paid by the loser to the party who correctly predicts the outcome of an event. See <http://www.collinsdictionary.com/dictionary/english/bet>.

The common law definitions of a “bet” as well as the Massachusetts definition strongly suggest that DFS would qualify as a “betting, gambling or wagering scheme” under PASPA where a sum of money is pledged on the outcome of a future unknown event. In DFS, such a sum is pledged on the future performance of the group of athletes that a participant drafts for his/her fantasy team in the hopes that those performances will score more points than the participant’s competitors.

Even accepting an argument that the terms are somewhat vague or subject to multiple interpretations, clarification is found in the legislative history of PASPA, by way of the Senate Committee report on the statute which states:

The prohibition of section 3702 applies regardless of whether the scheme is based on chance or skill, or on a combination thereof. Moreover, the prohibition is intended to be broad enough to include all schemes involving an actual game or games, or an actual performance or performances therein, including schemes utilizing geographical references rather than formal team names (e.g., Washington vs. Philadelphia), or nicknames rather than formal names of players.
S. REP. NO. 102-248 at 8 (1992).

This language clearly demonstrates that the statute was designed to have a broad scope applying to a wide swath of “schemes” regardless of the balance between chance and skill.

APPENDIX C

The specific UIGEA carve out language states:

the term bet or wager ... does not include ... participation in any fantasy or simulation sports game or educational game or contest in which (if the game or contest involves a team or teams) no fantasy or simulation team is based on the current membership of an actual team that is a member of an amateur or professional sports organization and meets the following conditions:

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 participants.
2. All winning outcomes reflect the relative knowledge and skill of the participants and are determined predominantly 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 any combination of such teams; or
 - b. Solely on any single performance of an individual athlete in any single real-world sporting or other event."

Adopting this language wholesale runs the risk of creating a host of additional undefined terms that will undoubtedly sow legal confusion in the same vein as PASPA. For example, UIGEA fails to define "a real-world sporting event" thus raising the question of whether such an event is an entire game, a quarter, an at-bat, a ball possession or some other fragment of time defined by the specific sport involved. Determining what qualifies as a "real-world sporting event" would necessarily affect

which sports could be offered as existing contests involving golf and NASCAR often focus on one tournament or race and under the UIGEA language no winning outcome can be based on a single performance in a single event.

Similarly, winning outcomes “determined predominantly by accumulated statistical results” is a problematic phrase. It is unclear what UIGEA is considering beyond statistical results to determine the winner even if statistical results are the “predominant” factor in such a conclusion. Additionally, the statutory language does not explain how many “statistical results” are sufficient for such a game or who determines which statistical results are appropriate on which to base a game.³¹

UIGEA was not originally drafted in an effort to legalize DFS and it has never been stress-tested through a rigorous legal analysis on the subject. UIGEA’s main thrust was as an enforcement act to address internet payment processors. While it may be helpful as an object lesson it does not have a “one size fits all” application as state legislation without significant clarification.

³¹ Given the number of data points generated during most sports and the development of advanced statistical analysis through such modes as sabermetrics, the term “statistical results” has nearly infinite potential.