

Kate C. Lowenhar-Fisher Member
klowenhar-fisher@dickinson-wright.com
Gregory R. Gemignani Member
ggemignani@dickinson-wright.com
Dickinson Wright, Las Vegas

Image: John Silliman / Unsplash.com

The impact of regulatory scrutiny on daily fantasy sports in the US

Back in the summer of 2015, daily fantasy sports ('DFS') had yet to fully arrive on the radars of US regulators and attorneys general, but had certainly attracted the attention of investors and players, even if its legal status was yet to be significantly scrutinised. By autumn that year, the emergence of attorneys general opinions on DFS shifted the legal risk around such activities; in the time since, a large number of states have seen their attorneys general opine on DFS' legal status or else have enacted state law to regulate or ban DFS in the state. A recent California court case, *Los Angeles Turf Club v. Horse Racing Labs*, which analysed whether a fantasy horseracing contest - on a site called Derby Wars - was a gambling event, has added to the legal complexity. Kate C. Lowenhar-Fisher and Gregory R. Gemignani of Dickinson Wright examine the effect of regulation on DFS, discuss the implications of *Los Angeles Turf Club v. Horse Racing Labs*, and assess the legal situation in regards to DFS in the US today.

Where things were in the summer of 2015

In the summer of 2015, the International Association of Gaming Advisors ('IAGA') held its annual International Gaming Summit ('Summit') in Vancouver, British Columbia. The Summit included multiple programs, including one centred on DFS. At that time, there were no authoritative court opinions and no attorney general ('AG') opinions regarding the legality of DFS. The DFS industry was growing rapidly through fundraising campaigns that drew investments from many professional sports leagues, famous sports team owners, and most large television networks.

A heated panel on DFS livened up the Summit that year. Representatives from the DFS industry claimed that DFS was profitable, unambiguously legal, and did not run afoul of US gambling laws. Licensed Las Vegas bookmakers countered that DFS was simply a form of sports betting and should be regulated accordingly. An experienced Las Vegas gaming attorney on the panel rounded out the discussion by pointing out that lack of enforcement (so far!) does not

make an activity legal. He added that as the DFS industry became increasingly conspicuous, enforcement action would become increasingly likely.

How things changed in the fall of 2015

In October 2015, Nevada was the first state to issue an opinion regarding DFS in response to inquiries from licensed gaming companies seeking to invest in DFS operators. Ultimately, the Nevada Attorney General's Office opined that DFS contests are sports wagering events that were permissible to conduct in Nevada pursuant to a sports pool operator's licence. The Nevada AG opinion was followed in November by an opinion of the AG of New York, which also held DFS to be a gambling game under New York law. The AGs of Illinois, Texas, Hawaii, Alabama, Georgia, Vermont, Mississippi, Tennessee, and Delaware each came to similar conclusions that DFS contests were gambling in their states.

The opinions of Nevada and Texas were particularly damaging because law enforcement officials specifically identified DFS contests as a form of

sports wagering. Soon, popular media in the US also began referring to DFS contests as a form of sports wagering. The critical problem for the DFS industry was that if the contests were deemed to be sports wagering, then the Wire Act would prohibit conducting DFS contests across state lines. Furthermore, DFS would be able to take place only in Nevada, Montana, Oregon and Delaware pursuant to the Professional and Amateur Sports Protection Act ('PASPA').

In an effort to counter the negative law enforcement opinions, the largest DFS operators launched an aggressive lobbying campaign to encourage states to legalise and regulate DFS. Simultaneously, DFS operators voluntarily agreed to cease any and all contests that relied on the athletic performances of any college athlete, which meant that the NCAA would no longer have standing to enjoin the activity pursuant to PASPA. The results of this effort have been mixed. In response to the aggressive political campaign, New York, Mississippi, and Tennessee enacted new state laws to regulate DFS and overturn adverse AG opinions. Colorado, Kansas, Arkansas,

Today the DFS industry occupies an area of significant legal risk. AG opinions in Nevada and Texas, among other jurisdictions, identify DFS contests as a form of sports wagering.

Virginia, Massachusetts, and Indiana enacted laws to regulate DFS, thereby effectively preempting any adverse state law enforcement opinions. Efforts in Washington State, Oregon, Nebraska, Minnesota, Illinois, Ohio, Pennsylvania, Delaware, Rhode Island, Vermont, North Carolina, New Hampshire and Maine have been unsuccessful so far, but are ongoing. Efforts in Iowa, Wisconsin, Michigan, California, New Mexico, Nevada, Arizona, Texas, Oklahoma, Hawaii, Louisiana, Alabama, Georgia, South Carolina, Florida, West Virginia, Kentucky, and Maryland have failed.

The first court opinion with an analysis
 Recently, a court in California analysed whether a fantasy horseracing contest was a gambling event in *Los Angeles Turf Club v. Horse Racing Labs* (CV 1509332, May 15, 2017). In this matter, Horse Racing Labs ('HRL') operates a site called Derby Wars. Derby Wars is a fantasy horseracing site, where players assemble a roster of horses running in multiple races. Rosters are scored and the player with the highest scoring roster receives a pre-determined cash prize. Los Angeles Turf Club, along with others in the horseracing industry, filed a civil racketeering action against HRL based on an assertion that the HRL contests were a form of wagering addressed by the Interstate Horseracing Act 1978 (the 'IHRA'). Because HRL did not follow the requirements of the IHRA, the claimants asserted, the HRL contests were an illegal form of betting.

HRL argued that the contests were contests of skill exempted from gambling prohibitions in California and elsewhere. This argument is based on HRL's evidence that to win the contests, participants must study and select a roster of horses that will outperform the rosters of other contestants. HRL argued that such skill contests were exempted from gambling laws, including horserace wagering laws. HRL further argued that its contests were exempted from the definition of a bet or wager under the federal Unlawful

Internet Gambling Enforcement Act ('UIGEA'), and, therefore, were not bets or wagers under other statutes such as the IHRA or state law. Finally, HRL argued that the IHRA only addresses pari-mutuel wagers and its DFS contests were not pari-mutuel wagers.

The Court assessed the arguments of the parties and determined that the IHRA applied to pari-mutuel wagers and other forms of wagering. Next, the Court looked at the UIGEA and determined that it did not preempt the IHRA or state law in determining whether the contests contained a bet or wager. Finally, it looked at whether the HRL contests were wagering under state law and the IHRA. The Court applied a long-standing definition of a bet or wager as "an agreement between two or more that a sum of money or some valuable thing, in contributing which all agree to take part, shall become the property of one or some of them, on the happening in the future of an event at the present uncertain and the stake is the money or thing thus put upon the chance." Essentially, wagering means staking something of value upon the outcome of an uncertain event the participants cannot control or materially influence for the opportunity to win something of value in excess of what is staked. Using this definition the Court held that the entry fees in the HRL contests were a wager akin to the wagers which form the 'pot' in poker. Having established the presence of a wager, the Court deemed the HRL contests to be a form of horserace wagering that was illegal absent compliance with the IHRA.

Where things are today

Today the DFS industry occupies an area of significant legal risk. AG opinions in Nevada and Texas, among other jurisdictions, identify DFS contests as a form of sports wagering. If the contests are deemed by a federal court to be sports wagering, then conducting the contests in interstate commerce violates the Wire Act and the Illegal Gambling Business Act, both of which are federal criminal laws. If the DFS contests are

contests that merely violate state gambling prohibitions other than sports wagering prohibitions as characterised in some law enforcement opinions, then offering the contests in interstate commerce to anyone in a state where such wagering is illegal will violate state law and the Illegal Gambling Business Act. As many operators still offer contests to residents of states with a law enforcement opinion that deems the activity to be unlawful gambling, there is an ever-present risk of prosecution.

Given the recent court opinion in California, there is a heightened degree of risk that the same analysis that was applied to Derby Wars will apply to DFS because the facts are virtually identical. However, the court opinion was focused on horseracing and the IHRA, and it is unlikely that any significant DFS operator will abandon the most populous state in the United States without trying to argue some distinguishing characteristic between Derby Wars and other DFS contests.

In spite of the rash of adverse AG opinions, there has been no apparent criminal prosecution of any DFS operator, even in states in which the AG of that state has issued an opinion that the activity is a form of illegal gambling. Likewise, there have been no actions for failure to pay wagering excise taxes, insider trading, or deceptive trade practices, all of which have been mentioned as potential areas of risk by law enforcement statements or industry analyst statements.

Therefore, while significant risk may exist for the DFS industry, very little of that risk has been realised by the industry. If or until such a risk is realised, it is likely the DFS industry will continue its march toward state regulation and focus on consolidation in an effort to turn investment funds into profitable operations.