REGULATORY MODELS FOR SPORTS WAGERING: THE DEBATE BETWEEN STATE VS. FEDERAL OVERSIGHT

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INTRODUCTION

The “legalization” of sports betting in the United States is only a beginning point for sports betting being available outside Nevada. The federal and state governments should address several issues regarding the structure and methods of regulating the activity. Thinking that the many key questions relating to a sports betting regime will answer themselves is unrealistic. Choices should be made on issues that are likely to be contentious. Chief among these matters is determining whether the locus of regulation should be in the federal government, left with the states, or involve both. Beyond that, important details relating to contest integrity, promoting competition and innovation, and spurring fan engagement will need to be considered carefully.

Like most forms of gaming regulation, the regulatory model(s) that emerge(s) will likely be a product of political compromise. The models we set out here are not meant to be an exhaustive list of possibilities. They do, however, offer a template for considering the objectives regulators and policymakers should keep in mind in establishing a regulatory system. Any regulatory system should seek to achieve the values and goals that are identified by policymakers as important. The more self-conscious policymakers are in identifying these values, the better the regulatory system is likely to be.

Before discussing the models, two foundational issues will supply necessary context. The first is a description of the historical relationship between the federal and the state governments as it relates to the regulation of gambling. Regulatory models that deviate from this association may create problems of implementation as the federal-state relationship is restructured.

1 This article is derived from an upcoming chapter of SPORTS WAGERING IN AMERICA: POLICY, ECONOMICS & REGULATION, by Anthony N. Cabot & Keith C. Miller (forthcoming Spring 2018 by UNLV Gaming Press).

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consideration of the advantages and disadvantages of the potential models of regulation.

I. HISTORICAL RELATIONSHIP BETWEEN THE FEDERAL AND STATE GOVERNMENTS

Before the passage of the Professional and Amateur Sports Protection Act ("PASPA"), federal policy towards gambling was relatively simple. Rather than preempting state laws, federal gambling laws were to aid states in enforcing their laws that prohibit gambling. There are several examples.

In adopting the Federal Wire Act, Congress in 1961 made clear its respect for the rights of individual states to regulate gambling within their borders. The Travel Act, the Wagering Paraphernalia Act, and the Illegal Gambling Business Act are laws enacted during the 1960s and 1970s that also illustrated the supplementary role of federal gambling laws. Congress passed these laws in response to the proliferation of illegal multistate gambling operations conducted by organized crime. The federal government intervened because states could not adequately investigate and prosecute criminal organizations that operated in multiple states. The creation of separate federal offenses based on a predicate state law violation gave the Federal Bureau of Investigation the authority to investigate and the Department of Justice the ability to prosecute national crime organizations.

These considerations also have application to the regulation of sports betting. Once again, a lack of resources or jurisdictional authority limits the ability of state governments to regulate interstate or foreign businesses. Federal intervention is necessary to achieve goals that are beyond the jurisdictional reach of the states. In the context of sports wagering, these goals include: (a) international criminal cooperation for the exchange of intelligence and information related to the investigation and prosecution of manipulation of sports results at national and international levels; (b) establishing common standards for extraterritorial jurisdiction and international extradition; (c) agreeing to collect, preserve and share evidence (including electronic data) with

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5 See United States v. Yaquinta, 204 F. Supp. 276, 277 (N.D. W. Va 1962) ("The purpose of the [Wire Act] is succinctly stated in Report No. 588 of the Senate Judiciary Committee of the 87th Congress, on July 24, 1961, as "* * * to assist the several States in the enforcement of their laws pertaining to gambling and to aid in the suppression of organized gambling activities by restricting the use of wire communication facilities.").
7 Id. § 1953.
8 Id. § 1955.
foreign governments relating to competition manipulation; and (d) agreeing to require licensed sports books to provide betting data to national and international data bases to detect criminal behavior.

Since the passage of the Interstate Horseracing Act (“IHA”), however, federal intervention into gambling regulation has become more prevalent. With this law, first passed in 1978,10 Congress exercised control over the economics of the sport of horseracing. The law requires that race books share a portion of each wager with the race tracks and the horse owners on whose racing events the race books were accepting wagers.11 The legislative history of the law indicates that Congress saw this revenue sharing as promoting the stability of horseracing and off-track betting in the United States.12 As a practical matter, the off-track race books have to negotiate a contract with the track to conduct wagering on the track’s races.13 Because both parties need the other to maximize profits they have relatively equal bargaining power. The Act also seeks to assure that horsemen receive fair shares of interstate wagers by including their consent as a “condition precedent” to the agreements.14

Congress’ intervention in horseracing may have relevance to sports wagering. PASPA prevented states from determining their policy towards gambling on sporting events involving humans, as the IHA did with sporting events involving horses. If in a system of widespread regulated sports betting, sports books had to pay to the leagues a portion of every bet, the IHA would be a valuable precedent.

11 To this end, the original version of the Interstate Horseracing Act (“IHA”) prescribed rules for “interstate off-track wager[ing],” which Congress defined as a “legal wager placed or accepted in one State with respect to the outcome of a horserace taking place in another State.” Id. § 3002(3).
12 Congress envisioned an interstate pari-mutuel scheme to ensure that states would “cooperate with one another in the acceptance of legal interstate wagering.” See id. § 3001(3).
13 The IHA governs the relationship between the OTB operators, licensed internet and interactive television horse race betting services, the tracks, the horse owners and trainers, and the state racing commissions. All other aspects of horseracing, such as licensing and policing, are left to the discretion of the various state racing or gaming commissions. Before an OTB operator can accept an interstate off-track wager, “consent” must be obtained from three parties: (1) the track; (2) the racing commission in the state where the track is located; and, (3) the racing commission in the state where the OTB operator is located. The use of the word “consent” should not mask the true intent of the Act, however. Consent comes with a price, either in the form of an agreement to provide wire information or a simulcast, or to conduct pari-mutuel wagering.
14 The IHA has met its original objective of assuring that the tracks receive a fair share of interstate wagers on races conducted at its track. The respective rights of the OTB operator and the track are well defined under the IHA. This usually includes provisions for the merging of pari-mutuel pools and the receipt by the OTB operator of the race simulcast and instantaneous transmission of all tote (i.e., wagering) and other track information. See 15 U.S.C. § 3004(a)(1).
PASPA and the IHA are consistent in one other important aspect. Neither act attempts to create a federal regulatory scheme over the gambling activity itself. In the case of PASPA, the intention was to create a national prohibition against state-authorized sports wagering. With the IHA, the intention was to assure that the race books compensated the parties that created the event upon which race books offered wagering. While the United States Supreme Court’s decision in the case brought by New Jersey challenging the constitutionality of PASPA may put to rest that federal effort to determine state policies toward sports betting, Congress may seek other ways to intrude on these state prerogatives.

The federal government has historically played no role in the discharge of the traditional regulatory functions of licensing, enforcement, and audit. It has, however, asserted regulatory authority over some aspects of casino operations, the most prominent being anti-money laundering laws. For example, casinos

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15 What is striking about the PASPA and IHA is that while both laws address sporting events with highly skilled athletes, their treatment of the activities is quite different. In the case of horseracing, Congress shows no concern for the impact of wagering on the integrity of the sport. Instead, Congress’ concern is to assure that the various stakeholders in the sport are fairly compensated when persons accept wagers on their events. No proof exists that horseracing is any more tainted with scandal than other sports. The only difference is that the powerful horseracing industry wants wagering on their sport and the powerful professional sports leagues want a ban on sports wagering that does not involve horses.

16 Money laundering is the process by which criminals transform the money that they receive from criminal activities into funds that appear to have been generated by lawful means and cannot be traced by law enforcement to their illicit sources. “Money laundering involves three steps. The first is placement, which involves changing the form of the funds into a less suspicious, more easily manipulated form. Placement is the most well-known phase of money laundering. Criminals, particularly drug dealers, tend to accumulate their money from the sale of drugs to customers in smaller denominations. [t]hese funds tend to be bulky and difficult to transport. Therefore, methods need to be devised to convert the smaller bills into larger bills, bank checks, money orders, traveler’s checks, or some other form of cash equivalent.”


“The next step is to layer the funds. Layering is the method by which criminals distance themselves from the converted funds. The idea is to provide a series of financial transactions that inhibit the ability of law enforcement to track the money back to their owner of source. This frequently involves wire transfers between bank accounts, often in foreign countries.”

Id. at 59.

“The final step is integration, which involves transferring the layered funds from the foreign country into a mainstream financial world in the US through a transaction that has legitimate commercial purpose.” Id. Using wagering operations for “placement” is different for land-based and internet operators. The latter generally are not set up to accept cash. Instead, they typically use a third-party intermediary to obtain money from the customer. In some cases, however, illegal internet operators have used runners to accept large cash deposits from patrons in
and sportsbooks must report certain currency payments and suspicious activity to comply with Bank Secrecy Act ("BSA") regulations promulgated by the federal agency called the Financial Crimes Enforcement Network ("FinCEN").\(^{17}\) Sports books must file Currency Transaction Reports ("CTR") for all cash transactions over $10,000, either individually or in the aggregate, in one gaming day.\(^{18}\) While all suspicious activity may not warrant a CTR because of the currency transaction value,\(^{19}\) the sports book must file a

person and establish on-line account wagering. The patrons will simply wager against the moneys held on account and at his request have amounts debited from the account and returned in cash to the patron in person. Wagering operations can assist in the layering process of laundering money. A value of involving wagering operations is that the funds can be disguised as winnings when, in fact, no “gambling” transaction has ever taken place. Take, for example, an unscrupulous operator in an unregulated environment. A drug dealer could set up multiple accounts with the operator. Some accounts result in the drug dealer “losing” all the deposited funds, while other accounts result in the drug dealer “winning.” The funds from the winning accounts are then transferred to an internet bank in the “layering” process. To anyone investigating the trail, the funds appear to be legitimate internet casino winnings. For example, if a patron bets $100,000 on one side of a football game in one account and $100,000 on the other side in a different account, then one account will show a large gain and the patron is only out the vigorish. In both scenarios, the account with the large gain will look like a legitimate gambling win. More pertinent to sports integrity, however, is when the criminals rather than simply using the wagering operations to launder money at the standard vigorish, attempt to use the markets to both launder money and make a profit by fixing the games on which they bet. See Emine Bozkurt (Member of the Special Committee on Organized Crime, Corruption and Money Laundering), Match Fixing and Fraud in Sport: Putting the Pieces Together, at 2 (Sept. 17, 2012), http://www.europarl.europa.eu/document/activities/cont/201209/20120925ATT52303/20120925ATT52303EN.pdf. The wagering industry is particularly suspect to layering because: high liquidity; is a cash business and has fluid cash flow; has easily accessible global markets; has significant unregulated markets; has a lack of harmony in regulations and a lack of cooperation between regulated markets; winnings are tax free in some jurisdictions and/or winnings can be easily transferred to other jurisdictions.

17 The forms used to report such activities are FinCEN Form 112: Currency Transaction Reports (CTR) and FinCEN Form 111: Suspicious Activity Report (SAR).

18 Besides the standard CTRs filed for a single currency transaction, casinos must file CTRs for reportable multiple transactions identified through the aggregation of daily records. As such, the sports book will periodically update records used to assist with customer verification to ensure their accuracy.

19 A sports book must have internal controls to detect suspicious activity, using a risk-based approach to the areas of products and services, customers, geographic areas, and transaction types.
Suspicious Activity Report (“SAR”) if it observes a suspicious activity whether attempted or completed and involving $5,000 or more in funds or other assets.20

II. FACTORS TO CONSIDER

This section sets out seven primary factors that policymakers can consider in evaluating different models that assign control over the regulation of sports wagering to the federal government, the states, or a combination of both. Then, the relevant factors will be used to examine the advantages and disadvantages of each model and, in some cases, the political dynamics of gaming regulation that may favor or disfavor a model.

Regulation can promote inefficiencies in a market in several ways: by setting prices above competitive rates, restricting information that consumers use to price shop, and by creating “barriers to entry.” Governments, the public, and the casino industry should understand the consequences of regulation and the factors that produce those consequences. An awareness of the costs of regulation on price and innovation can help to make regulation more efficient and the price of the gaming product lower.

A. Barriers to Entry / Pricing

Most common among the indirect economic consequences of regulation is the creation of barriers to entry. The absence of barriers to entry helps to promote competitive market models. Markets are fluid; demand can rise and


• Complete customer information, such as name, permanent address, government-issued identification number, date of birth and patron account number
• A narrative that describes the suspicious activity including:
  describing the suspicious activity in a complete and chronological way;
  identifying “who,” “what,” “when,” “why,” “where,” and “how”;
  identifying whether the transaction was attempted or completed;
  noting any actions (taken or planned) by the sports book, including any internal investigative measures to maintain records of the suspicious activity; and
  including contact information for persons at the sports book with additional information about the suspicious activity.
fall. If demand increases and prices do not change, excess demand would occur, and prices would inevitably rise. With higher prices, firms supply more, and prices may rise until supply increases. A common means of increasing supply is when new participants enter the market because they are attracted by the potential return on investment. If barriers to entry inhibit potential entrants, existing market participants can enjoy the benefits of higher prices and, most likely, positive economic profits.

The costs and burdens of regulatory compliance on the sportsbooks can create barriers to entry that have a significant impact on pricing and competition. An unintended economic consequence of gaming regulation is higher prices for gaming products. Regulatory compliance costs include the direct costs of government regulation, as well as the indirect costs that come from any economic inefficiencies created by regulation. In contrast, illegal sportsbooks have minimal regulatory costs, low or no taxes, and high liquidity. This permits them to offer lower “pricing” in the form of better odds than the regulated sportsbooks.

That regulation has an economic impact by restricting entry does not mean the regulation is necessarily good or bad. Achieving policy goals may be worth the costs of regulation. For example, the legal requirement for medical doctors to obtain a license to practice is intended to protect the public from possible harm to their health. The consequences that unqualified persons may poorly administer medical treatment may justify limiting the number of medical providers. It will, however, raise the costs of medical services.

Gaming licensing is supposed to create a barrier to entry. Few would dispute that keeping persons who are likely to cheat customers or who are members of organized crime from entering the industry is a desirable goal. The imposition of reasonable costs is necessary to achieve such goals. If a jurisdiction’s licensing system were perfect, only those who fit the government’s standards would obtain a license. Licensing, however, cannot be done with total efficiency because the process erects barriers relating to costs, risks, delays, or potential adverse publicity that may keep out suitable potential entrants.

State licensing requirements also can create absolute barriers to entry. If sportsbooks could only operate in casinos or racetracks, that prevents other qualified companies from providing services in that state. This restricts a bettor’s choice of potential sportsbooks and will almost certainly produce higher prices to the detriment of the bettors and the advantage of the illegal offshore bookmakers.

Moreover, a lack of regulatory uniformity between governmental entities also raises costs and barriers to entry. For example, if states individually regulate sports wagering and each requires a separate license, the costs of getting licensed in each state favors companies with large capital resources and creates a significant barrier to entry for other companies. The same is true when sportsbooks must operate within numerous regulatory systems having
dissimilar regulations, standards, processes, and enforcement. Uniformity in regulation, on the other hand, lowers entry barriers for new companies and reduces costs.

B. Liquidity

Liquidity in this context refers to the amount of money wagered (handle), which is functionally related to the amount of money that players can wager and win. Greater liquidity lowers pricing because fixed costs are spread over a larger base. It also increases the choice of wagers because sportsbooks can offer less popular wagers if a sufficient market exists to justify the cost of implementation. Lower liquidity on the other hand may result in the sportsbooks setting lower bet limits to manage risk better.21

High liquidity in illegal markets makes competition manipulation more difficult to detect. This is because the amounts wagered from corrupt sources may still not be enough to trigger concerns of unusual activity. On the other hand, high liquidity is good for regulated markets because the more data that is subject to analysis and early warning systems, the more likely that corruptors will be deterred or discovered. As one commentator noted:

Attempts to reduce liquidity by imposing restrictions in domestic betting markets may, if anything, prove counter-productive. For example, if certain bet types are prohibited, or if domestic operators are constrained to offer ‘unattractive’ odds, serious bettors, who are responsible for a disproportionate share of volume, may shift their activities to the international market, further enhancing liquidity in the part of the market where regulatory supervision is weak or non-existent. This appears to be the opposite of what is needed. There is a prima facie argument for improving choice and value for bettors willing to trade in a supervised environment because, where they do so, this will reduce liquidity in the unsupervised sector.22

C. Revenue Potential

This factor looks at which model is most likely to result in the highest generation of gross revenue, which, after expenses, leads to net income and taxable revenue. Revenue potential is important because it impacts the number of potential competitors and their willingness to commit capital. It also affects

21 See discussion infra Part III.
the ability of the government to maximize tax revenues based on the net income of sportsbooks.

D. Fan Engagement

Fan engagement is a phrase used to describe the behaviors that followers of a sport, team, or athlete engage in. This includes such things as watching games in person, on mobile devices or television, buying team or athlete-related products, reading sports print or digital media, and communicating with others regarding their interests or experiences. Sports leagues have a keen interest in sports wagering as a method to increase fan engagement. Television ratings for most sports have declined, for reasons that are not clear. One possibility is the “cord-cutting” that has been a result of the growth of mobile technology and viewing options for viewers. In any event, one of the reasons the leagues have been supporters of fantasy sports, and more recently, daily fantasy sports, is a belief that having a financial stake in a sporting contest promotes “fan engagement.” This may be another way of saying that people may watch a


24 See infra note 26 and accompanying text.

25 The ratings decline for the NFL has been a well-documented trend over the past several years and has continued into the first half of the 2017 season. Through the first six weeks of the 2017 NFL season, networks have witnessed a decline of 7.5 percent compared to the same time period in 2016. Compounded with the eight percent decline in rating in 2016 compared with 2015, the National Football League has lost a substantial amount of television viewers over the last couple years. See Scooby Axson, NFL TV Ratings Down 7.5 Percent, SPORTS ILLUSTRATED (Oct. 18, 2017), https://www.si.com/nfl/2017/10/18/nfl-television-ratings-decline. Ratings decline has not been limited solely to professional football, as the NBA has experienced a decline in viewership on their regional sports networks. See John Ourand & John Lombardo, NBA’s RSN Ratings Down 15 Percent This Season, SPORTS BUSINESS DAILY (Feb. 20, 2017), http://www.sportsbusinessdaily.com/Journal/Issues/2017/02/20/Media/NBA-RSNs.aspx.

26 Cord cutting has accelerated in recent years with “cord cutters” in 2017 far outpacing previous projections. It is estimated that by 2021, there will be a ten percent decline in cable subscriptions from 2016 numbers. See Todd Spangler, Cord-Cutting Explodes: 22 Million U.S. Adults Will Have Canceled Cable, Satellite TV by End of 2017, VARIETY (Sept. 13, 2017, 3:00 AM), http://variety.com/2017/biz/news/cord-cutting-2017-estimates-cancel-cable-satellite-tv-1202556594/ (noting that cord cutters have increased thirty-three percent from 2016, up to over 22 million former cable and satellite TV subscribers).

game they are not otherwise interested in, or that they may continue to watch a game after the overall result is clear, when they stand to win or lose money on the contest.

Until recently, the leagues have substantially opposed fan engagement produced by single-game wagering. While this view is evolving, single-game betting is not the only way to promote engagement, as fantasy sports has illustrated. The leagues are seeking new and innovative ways for fans to interact with the games, and the athletes, to promote increased viewership and interest in the sports. States might be incentivized to develop novel forms of wagering that will promote liquidity for the sports betting markets and perhaps boost viewership. This will inure to the benefit of the sports leagues as well as those involved in operating these new sports betting products. While mere single game wagering alone is a vehicle for increased fan engagement, other wagering products designed to be more interactive with the player might also have appeal. These wagering products would serve the same function as fantasy sports did for skill-based contests.

Fantasy sports was a disruptive product that changed the way that sports leagues and media outlets delivered sports to the consumer. For example, the “RedZone” is a television channel that switches from stadium to stadium to capture highlights of significant plays in the games, and offers live coverage when one team is threatening to score based on its field position. The NFL and media partners designed this channel for the fantasy player.28 Other innovative sports betting products will be an essential part of enhancing fan engagement by embracing the way fans consume sports. It is likely that these products will surpass traditional sports wagering in encouraging engagement.

E. Speed to market

Speed to market has two aspects. The first is how quickly operators can offer a sports wagering product to the public in places where legal. The second is how quickly individual competitors can bring new products or product innovations to market considering regulatory hurdles such as product approvals.


28 Nick Greene, RedZone is the Cause of and Solution to All of the NFL’s Problems, SLATE (Sept. 17, 2017, 8:18 PM), http://www.slate.com/blogs/the_slatest/2017/09/17/redzone_is_the_cause_of_and_solution_to_all_of_the_nfl_s_problems.html.
F. Effectiveness

Effectiveness looks at whether the regulatory processes accomplish the public policy goals. Four common ways that regulatory processes fail to meet their goals are knowledge failure, instrument failure, implementation failure, and motivation failure.\(^\text{29}\) Knowledge failure occurs where the government has insufficient knowledge: (a) to identify what the regulation is attempting to accomplish, and (b) to design appropriate laws or regulations or identify non-compliance.\(^\text{30}\) Instrument failure is where the laws or regulations (the instruments) are inappropriate or unsophisticated.\(^\text{31}\) Implementation failure occurs when enforcement mechanisms fail to accomplish policy goals.\(^\text{32}\) This can occur because the government does not have the knowledge, competence, resources, or money to regulate effectively. Motivation failure takes place when those regulating are insufficiently motivated to enforce the law because of inaction or corruption.\(^\text{33}\)

G. Political Viability

States are hesitant to give up control over gambling to the federal government. Part of this is a fundamental states’ rights argument. Another factor, however, may be to protect their home state industries. For example, exclusive licenses to conduct sports wagering are likely to go to the state lottery in a state with a dominant state lottery and a weak or non-existent casino industry. Similarly, in states with a politically powerful casino (or horseracing) industry, licenses may be issued only to those companies that already have licenses. The political strength of casinos, horse race interests, and lotteries within a state can complicate a uniform federal approach to regulation.

III. CATEGORY ONE — STATE REGULATORY APPROACHES

Within a framework of state-by-state regulation, there are several possibilities. Each would draw from models of regulation for other forms of gambling.

A. State Model #1: The Status Quo

A basic state regulatory approach would be a purely intrastate system where an operator would need to have a physical presence and obtain a gaming license in the specific state to offer sports wagering there. The federal

\(^{30}\) *Id.*
\(^{31}\) *Id.*
\(^{32}\) *See id.*
\(^{33}\) *See id.*
government’s role would be limited to providing enforcement for interstate or foreign crimes, which does not extend to regulation. As noted earlier, for the most part, this is the existing approach that is used for casino wagering. The trade association for the casino industry contends that maintaining the current division of responsibilities between the state and federal governments is the best structure. This model preserves both the status quo and where applicable, the exclusivity of the casinos’ existing licenses.

Benefits might include:

- **Speed to Market.** States already have regulatory apparatuses in place that could create the foundation for sports regulation. For example, New Jersey Governor Chris Christie stated that if New Jersey won the Supreme Court case its casinos and racetracks could begin offering sports wagering within two weeks because the state had prepared for the contingency. Other states could quickly emulate Nevada or New Jersey by piggybacking off their existing regulatory processes. Nevada uses the same licensing, accounting, audit, and enforcement agents to regulate both the casinos and sports books. Due in large part to the limitations set by PASPA, Nevada has enjoyed a substantial head start over other states and has a well-developed sports wagering system. Consequently, states may initially look to Nevada for how a model of the regulation of sports wagering should operate within existing regulatory structures. But this would likely evolve as states began to improve on and adapt the Nevada model. Moreover, states could develop their regulatory structures as “laboratories” for other states to learn from. This process of learning from the examples of other states is one of the most widely-valued characteristics of our...
federal structure.38

- **Effectiveness of Wagering Integrity.** States would have autonomy to tailor a sports wagering system that fit their own peculiar set of values and regulatory goals; the tradition of local control of gambling would be promoted. Finally, states might be more responsive to technological change and would be able to adapt more quickly to proposals for innovation.

- **Political Viability.** A state model may be the only viable option given the difficulties of enacting legislation in an intensely partisan Congress. Drawbacks might include:

  - **Potentially High Barriers to Entry Due to High Compliance Costs.** Companies with a presence in multiple states have extremely high compliance costs. For example, if states did not limit sports book licenses to their existing casinos, racetracks, or tribal gaming operations, a company wanting to obtain licenses nationwide would be in the same position as manufacturers of gaming equipment. A licensed manufacturer of slot machines may need over 100 gaming licenses between state and tribal governments to sell their wares in the United States. Moreover, the technical standards for sports book systems and methods for communicating remotely with bettors may differ among jurisdictions. If, for example, states required functionality such as computer servers and key personnel to be physically located in the state, massive inefficiencies that raise costs and create significant barriers to entry would exist. These costs increase prices to the betting public and affect the legal industry’s ability to compete against illegal off-shore sportsbooks which can offer better odds because they have lower costs.

  - **Absolute Barriers to Entry Based on Licensing Criteria.** Politics can play a significant role in shaping a state’s regulatory policy. Those influencing policy may promote a protectionist (“ring fence”) approach where states have the incentive to implement laws that would benefit existing operators. An existing system can serve as an anticompetitive tool that allows existing casinos, racetracks, and tribes to maintain their exclusive licenses to the detriment of other competitors that may be better financed, have superior technology and experience, and have more innovative products. For example, New Jersey’s sportsbook law limits the granting of licenses to existing casinos and racetracks, neither of which have experience in sports betting. This absolute barrier to entry may stifle innovation and create uncompetitive odds that could disadvantage the sports betting public.39

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38 See New State Ice Co. v. Liebmann, 285 U.S. 262, 311 (1932) (Brandeis J., dissenting) (“[A] single courageous State may, if its citizens choose, serve as a laboratory; and try... experiments without risk to the rest of the country.”).

39 Protectionism’s harm on consumers has long been identified and analyzed by economists. See Robert Z. Lawrence & Robert E. Litan, *Why Protectionism...*
• Placing Small States at a Disadvantage. A small state would have the same fixed costs as larger states in establishing the regulatory infrastructure that is essential to the proper regulation of sports wagering. These costs include adequately trained personnel such as licensing agents, audit and accounting staff, and enforcement agents, as well as equipment. Small states would face liquidity problems as small betting pools produced low revenues, fewer bet options, and higher pricing. All this would damage the ability of a small population state to offer a competitive range of sports wagering products.

• Difficulties of Ensuring Sports Integrity. A state-centric approach may complicate if not frustrate the pursuit of sports integrity. Regulatory structures in place to protect the integrity of casino gambling have limited application to sports wagering. States and tribes have vast experience in regulating land-based gaming including casinos and gaming devices outside of casinos. The regulation of wagering integrity and sports integrity, however, is very different. Regardless of whether the government is regulating casinos to protect the bettor, maximize taxes, or create jobs, a standard policy goal of every regulatory system is to assure the honesty of the games offered to the public. Casino patrons are susceptible to fraud if an unscrupulous casino operator uses cheating methods to assure that a random event does not determine the gambling contracts. A dishonest casino can cheat the players by predetermining or influencing the result to its advantage. Gamblers who are cheated are unlikely to play at the casinos; this impacts taxes, jobs, and the general economy of the jurisdiction. A casino operator is honest if it offers games whose determinative outcomes are random. Given the importance of honesty to the gaming industry, governments that regulate casino gaming implement multi-faceted regulatory schemes such as licensing, technical standards, extensive testing, field observation and review, periodic audit and internal control requirements.

Sports and casino wagering share similar aspects. Legally, all wagers are contracts; the price (amount won or lost) is honored according to the terms of the contract when the bettor and a bookmaker enter it. The distinctive part of a wagering contract is that promise of performance is based on a future contingent event (the outcome of the casino game or the sports competition) not under the control of the casino or sports book, on the one hand, or the bettor, on the other. After that, whether the sports book or the casino must fulfill its promise to pay the bettor is dependent on the terms of the bet and the outcome of the future contingent event, either the casino game or sporting event. The difference between casino wagering contracts and sports wagering contracts is that state regulators tightly
control the regulation of the future contingent event in casino contracts. Assuring the honesty of the underlying event that determines the outcome of a sports wager, in contrast, is much different. These uncertain contingent events do not occur in the casino nor typically the jurisdiction where the casino is located. As a result, the integrity of the sporting event is largely outside the control of the state regulators. Therefore, state governments must accept the risk that those who place sports wagers with the sportsbook could be the victim of fraud by competition manipulation.

- **Limited Fan Engagement.** State-ringed sports wagering will likely produce smaller, disaggregated wagering pools. This will affect traditional types of wagers, such as single-game wagering, because it limits the number of wagering opportunities, creates greater odds fluctuations, and limits liquidity. However, the bigger impact will be on new products designed to increase fan engagement. As online poker experienced, state-based ring fencing produced smaller betting pools and poker game options that were not attractive. A similar result may occur with sports wagering where more immersive game products may only have viability with high liquidity.

B. **State Model #2: State Regulation with Open Markets**

Under this model, the regulation of sports betting would be the responsibility of the respective states. Unlike State Model #1, however, any operator who submitted to the licensing authority of a state could offer sports wagering in the state. In other words, the operator would not be required to have a physical presence in the state. This approach would resemble that used in the daily fantasy sports industry. In the United States, a firm can offer fantasy sports in multiple states, thus creating the liquidity necessary to operate a viable business. However, the company must comply with licensing and other standards imposed by the individual states. About a dozen states allow daily fantasy sports companies to offer their national contests within their state provided they comply with state laws for licensing, operational requirements, and consumer protections.

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41 Ryan Rodenberg, Daily Fantasy Sports State-by-State Tracker, ESPN (July 26,
Benefits of such an approach would include:

- **Barriers to Entry.** Barriers to entry would be reduced compared to the first state model because operators can determine which states they want to operate in based on factors like regulatory burden, costs, and business potential. Non-traditional gaming companies would have the opportunity to develop innovative forms of sports wagering in states they choose to operate in. Because companies would be subject to licensing and regulations in each state where they do business, however, the model does not guarantee uniformity. This will raise costs and potentially result in new products being either slow to market or only being offered in certain states.

- **Increased Liquidity.** While sports wagering is not as dependent on liquidity as daily fantasy sports, a non-national approach makes it difficult for small states to offer competitive pricing and hurts the ability of innovators to offer new products that have the prospect for higher fan engagement. This model reduces but does not eliminate the problems created by ring-fencing states and permitting intrastate wagering only.

- **Speed to Market.** States can determine how quickly to license and permit operators to access their markets. A new company may choose states with the fastest and least expensive regulatory path to licensing and operations and then expand to other states as it has resources to do so.

- **Fan Engagement.** Unlike model one that ring-fences activity into a particular state, this model allows companies to increase liquidity by leveraging multiple markets. This may promote innovative products that work better with higher liquidity or a more diverse fan base.

- **Effectiveness of Ensuring Wagering Integrity.** Like State Model #1, this model relies on states to ensure wagering integrity. As most states already have some form of gaming regulation, this model should be efficient and effective to ensure wagering integrity.

Drawbacks might include:

- **Barriers to Entry.** Like State Model #1, entities wanting to offer sports betting in multiple states will have to obtain licenses in each of them. Therefore, licensing becomes expensive. Likewise, varying audit, accounting, operational and technical rules in states are burdensome and deter all but the most heavily capitalized companies from entering state markets.

- **Ineffectiveness of Ensuring Sports Integrity.** This model does not alter the concerns raised for State Model #1 regarding ensuring sports integrity.

- **Political Viability.** This model is based on an open market. Companies without ties to a particular state, such as owning or operating a racetrack or casino, would have access to the sports wagering market. Casinos, tribes, 2017), http://www.espn.com/chalk/story/_/id/14799449/daily-fantasy-dfs-legal-your-state-state-state-state-look. Nevada is the only exception that requires ring-fencing — which effectively eliminates any prospect for a viable industry.
and racetracks with powerful lobbies, or states with an influential state lottery, are likely to fight this approach.

C. State Model #3: State Regulation with Reciprocity

This model subjects operators to the regulatory authority only in the states in which they conduct operations and maintain servers, but allows them to accept wagers from bettors in any state that has authorized sports wagering. This is similar to how the Interstate Horseracing Act works in practice. According to the popular interpretation of that law, a company wishing to engage in account-based wagering on horse races must obtain a license from a state that regulates that form of race wagering. The company has the choice of about twenty states that license race book operators. After obtaining this license, the race book can accept wagers from any state where betting on pari-mutuel horseracing is legal, which includes about thirty-six states.

Benefits of such an approach would include:

• **Lower Barriers to Entry.** The lowered regulatory burden of having to obtain a single license and comply only with the laws and regulations where a company is licensed would make it easier for operators to get to market.

• **Liquidity and Revenue Potential.** This state model provides the greatest liquidity because an operator can decide which jurisdiction to obtain a license and, after obtaining a license and all other necessary approvals, have access to the liquidity in all other states that permit sports wagering.

• **Speed to Market.** This state model provides the quickest speed to market because an operator can decide which jurisdictions to obtain a license. After obtaining a license and all other necessary approval the operator would have access to all other markets. This would stoke competition between states to create regulatory systems that can issue licenses expeditiously and provide for the least costly regulatory burdens.

• **Fan Engagement.** Like State Model #2, this model allows companies to increase liquidity by offering wagering in multiple markets. This liquidity will contribute to new products that may increase fan engagement.

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42 Interstate Horseracing Act of 1978, 15 U.S.C. §§ 3001-07 (2012). The Interstate Horseracing Act (IHA) was passed to “regulate interstate commerce with respect to wagering on horseracing, in order to further the horseracing and legal off-track betting industries in the United States.” There is a general prohibition on “interstate off-track wager[ing],” but there are exceptions for simulcast wagering with consent from the local jurisdiction.

Drawbacks might include:

- **Political Viability.** States might be wary of permitting wagering in other jurisdictions where sports integrity and patron protection provisions are inadequate.

- **Lack of Uniformity.** Conflicts between state laws would complicate operations and revenue sharing between states.

- **Ineffectiveness of Ensuring Wagering Integrity.** Operators would migrate to states with the lowest taxes, least comprehensive licensing standards, and fewest regulatory hurdles. These varied licensing standards can produce a “race to the bottom” among states. That is, to attract gambling companies, states may relax licensing standards so that they are more attractive than competing states. This is not a phenomenon limited to the gaming world. States often vie to attract or retain businesses by offering weakened environmental rules, property tax abatements, and lowered wage scales for workers. Although business competition is a hallmark of a capitalistic system, the success of regulated gambling depends upon integrity and public perceptions of integrity. Overly aggressive competition among states may undermine these critical objectives.

- **Ineffectiveness of Ensuring Sports Integrity.** Effective standards of sports integrity would be challenging to implement.

D. State Model #4: Liquidity Created by Interstate Agreements

This approach would share most of the characteristics of State Model #3, but it would be based on a compact model. That is, operators could accept wagers from patrons in states that had entered an agreement with other states.

Benefits of such an approach would include:

- **Liquidity.** Because it is based on the model used for internet poker and certain lottery products (like Powerball), there is some familiarity with how it would operate. Even though the four states that have legalized poker have reached an agreement to share liquidity, this has not made the activity especially lucrative. Greater liquidity, where states with a significant

44 See discussion of State Model #2, supra Part III-B.
combined population participate in the compact process, is likely necessary. As more states decide to legalize poker, this liquidity may develop. However, the slow rollout prevented poker sites from offering the products that the public wanted. National efforts to engage fans of poker through television and other media were not attached with opportunities to play and increase skill.

- **Effectiveness of Wagering Integrity.** States would have primary responsibility for regulating the operators in their state. The individual states would also have the power to enter or not enter compacts with other states. States would have the discretion not to allow operators from a state where regulatory oversight is lacking. This prevents race-to-the-bottom concerns where operators would otherwise be attracted to the states with the lowest taxes and least regulation. Moreover, compacts could be worked out between states according to the specific values and interests of the state.

- **Barriers to Entry.** Because an operator would not have to obtain a license in every state, barriers to entry would be lower than State Model #1 that only permits intrastate wagering.

Drawbacks might include (in addition to those noted in State Model #3):

- **Speed to Market and Political Viability.** Compacts would need to reconcile difficult issues of regulation, taxation, licensing, and revenue sharing. These differences may prevent or delay the implementation of a multistate system. As an example, though Nevada authorized internet poker in 2013, and New Jersey authorized internet poker in 2010, the states did not agree to a compact until 2017. Moreover, some larger states, like California, which has significant liquidity on an intrastate basis, may be hesitant to open its market to operators from smaller states.

### IV. THE FEDERAL APPROACH

#### A. The Federal Model – Exclusive Federal Jurisdiction

One plausible model of regulation would have the federal government as the regulator of sports wagering. A federal law would set out the terms of licensing and regulation, and direct a federal agency or entity to administer the law, promulgate and enforce regulations, and coordinate regulation with states.

Under this approach, states would choose to opt in, or not. That is, no state would be required to offer sports betting.\(^{49}\) A state choosing to participate,

\(^{49}\) States that do not permit commercial or tribal gambling are: Arkansas, Georgia, Hawaii, Kentucky, New Hampshire, South Carolina, Tennessee, Utah, Vermont, and Virginia. 2016 *State of the States*, AM. GAMING ASS'N, https://www.american-gaming.org/sites/default/files/2016%20State%20of%20the%20States_FINAL.pdf (last visited Mar. 12, 2018); Gambling has always been the purview of the states as PASPA is “the only federal law in history” regulating states’ regulation of
however, would be subject to the federal statutory regime.

Some benefits of this approach include:

- **Lower Barriers to Entry.** Compliance costs for companies would likely be lower compared to a non-uniform system. For example, licensing of companies and principals would be a one-time experience (at least initially), rather than the serial approach that most state-based models would produce. Similarly, the burdensomeness of varying state audit requirements would be eliminated. A single template for audit and accounting would streamline the process and reduce costs, and business planning would be enhanced by a uniform and straightforward federal taxing structure. A system could be created for sharing tax revenues with states. Reduced entry barriers would allow for companies to get to market quickly. Also, having to satisfy only one set of regulatory requirements would promote the emergence of non-traditional gambling companies; this would spur competition and innovation.

- **Increased Liquidity.** Having a unified network of the opting-in states would promote liquidity. Companies would have a single market in which all gaming proceeds would be pooled.

- **Fan Engagement.** A national liquid market with fan diversity and low barriers to entry is the best incubator for innovative products that are likely to produce the highest degree of fan engagement.

- **Effectiveness of Ensuring Sports Integrity.** The consistency of standards and enforcement from a federal system of regulation would implicate several aspects of a sports betting structure and help to serve important public policy objectives. Increasingly, the integrity of contests held in the U.S. is not just a matter of regulating bettors in the U.S. Illegal sports gambling markets in Asia have a connection to contest manipulation, and though their influence may not have affected U.S. betting markets, that could change. International cooperation is essential to address match fixing of contests held inside and outside the U.S. A federal system that would facilitate the collection of data so that threats to game integrity could be quickly identified and acted upon by federal law enforcement offers efficiencies that state regulation could not achieve. This may be among the reasons the major sports leagues in the U.S. seem to

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50 A patchwork of regulations and taxes greatly complicate business for companies as evidenced by the current experience of daily fantasy sports companies. See Dustin Gouker, Fantasy Sports Industry ‘Deeply Concerned’ With $50K Fee in Virginia Law, LEGAL SPORTS REPORT (Mar. 8, 2016, 8:04AM) https://www.legalsportsreport.com/8915/fsta-pushes-back-on-dfs-fees/.

favor a centralized system of regulation.\textsuperscript{52} Likewise, states are at a disadvantage in developing laws and regulations that would curb insiders from acting on information not available to the betting public. While states could share information on suspected betting irregularities by insiders, a centralized regulatory system would likely be more effective in detecting such activity. This has been one of the strengths of the manner in which securities are regulated at the federal level.\textsuperscript{53}

The Securities Exchange Commission (“SEC”) was created by the Securities Exchange Act of 1934 “to restore investor confidence in our capital markets by providing investors and the markets with more reliable information and clear rules of honest dealing.”\textsuperscript{54} Prior to the establishment of the SEC, regulating the honesty of the securities markets was left to the state governments through the creation of state regulatory schemes known as “Blue Sky” laws. These proved ineffective as stock promoters complied only with the laws of the states with the least regulation or the most corruption and used that as a basis for offering the stocks on a national basis.\textsuperscript{55}

Securities regulation and sports wagering have striking similarities. Both concern the regulation of exchanges involving contracts where the purchaser/bettor is attempting to earn profits based on a future contingent event. In both markets, the government is interceding into the markets to

\textsuperscript{52} Adam Silver, Legalize and Regulate Sports Betting, N.Y. TIMES (Nov. 13, 2014), https://www.nytimes.com/2014/11/14/opinion/nba-commissioner-adam-silver-legalize-sports-betting.html (“Congress should adopt a federal framework that allows states to authorize betting on professional sports, subject to strict regulator requirements and technological safeguards. . . Without a comprehensive federal solution, state measures such as New Jersey’s recent initiative will be both unlawful and bad public policy.”).

\textsuperscript{53} The United States Government regulates securities primarily through the Securities Act of 1933, 15 U.S.C. §§ 77a-77aa (2012). The Securities Act has two basic objectives: (1) “[R]equire that investors receive financial and other significant information concerning securities being offered for public sale;” and (2) “[P]rohibit deceit misrepresentations, and other fraud in the sale of securities.” See What We Do, U.S. SEC. & EXCHANGE COMM’N, https://www.sec.gov/article/whatwe do.html#laws (last visited Mar. 12, 2018); States also have authority to regulate securities within their state. These laws, known as “Blue Sky Laws,” are often modeled on their federal analog. Because of the overlapping and duplicative nature of many of these state laws, some have called for an entire, or field preemption, of state regulation of securities. See Rutherford Campbell Jr., The Case for Federal Pre-Emption of State Blue Sky Laws, THE HERITAGE FOUND. (Feb. 28, 2017), http://www.heritage.org/markets-and-finance/report/the-case-federal-pre-emption-state-blue-sky-laws.

\textsuperscript{54} 15 U.S.C. § 78a; What We Do, supra note 53.

protect the honesty of those contracts. Because the security markets, like
the sports markets, exist on a national (and international) level, state
regulation alone is inadequate.

States were unwilling to concede power to regulate the securities
markets until after the stock market crash of 1929. While the SEC has
faced criticism for both overregulation and under regulation, no serious
discussion exists that it is not a better system than what previously existed
under state control or that it should be dissolved. Ultimately, a centralized
system has significant advantages.

The federal/national approach would also have potential shortcomings:

• **Effectiveness of Ensuring Wagering Integrity.** While there is a
  prominent federal role in areas such as securities regulation and civilian
  aviation, Congress has no real expertise in establishing gaming regulatory
  regimes. The most recent effort to address sports betting — the Unlawful
  Internet Gambling Enforcement Act of 2006 (“UIGEA”) — is a deeply
  flawed law.\(^{56}\)

  No likely or appropriate federal entity exists where the regulatory
  locus would reside. A lack of experience and expertise for establishing a
  regulatory regime could impair achievement of the positives listed above.
  The “learning curve” for the new regulatory entity could lead to slow
  implementation which would frustrate potential market entrants.

  However, some federal agencies can serve as models. Agencies such
  as the SEC and Federal Aviation Administration discharge traditional
  administrative regulatory functions like licensing, enforcement, testing, and
  audits. As discussed above, the SEC may be the closest parallel both in
  mission and history.

  Finally, especially with the creation of a new regulatory body, there is
  a tendency to over-regulate. That is, the new entity might fulfill the
  standard view of the federal government as a bloated bureaucracy which
  stifles innovation and competition by imposing burdensome regulations.
  
  • **Speed to Market.** Nothing about a model of federal regulation supports
    an idea that market entry could be handled more expeditiously than with a
    state system.
  
  • **Political Viability.** The current dysfunction of Congress inspires little
    confidence that it can establish a workable system, especially since

\(^{56}\) 31 U.S.C. §§ 5361-5367 (2012) (prohibiting gambling businesses from
knowingly accepting payments “in connection with the participation of another
person” in “a bet or wager . . . which involves the use . . . of the Internet . . . [and
that] is unlawful under any applicable Federal or State law”). The criticism of
UIGEA has been deep and wide: See I. Nelson Rose, Viewpoint: The Unlawful
Internet Gambling Enforcement Act of 2006 Analyzed, 10 GAMING L. REV. 537,
538 (2006); I. Nelson Rose, Congress Makes Sausages, 11 GAMING L. REV. 1, 1
(2007).
decentralization of government functions is accelerating. Moreover, states will strongly object to being taken out of the regulation of sports betting and emphasize that regulation of gambling is typically left to the states. The state of Nevada, with its mature sports betting market, would not quietly accept being displaced by a federal system of regulation.

B. Mixed Federal and State Authority Model

1. Assigning Responsibilities for Sports Integrity to the Federal Government and Wagering Integrity to the State Government

A variation on the first model would still require federal legislation. States opting in would be required to demonstrate compliance with a template of regulation established by federal law. States would be in charge of wagering integrity through regulation in their state and would be empowered to tailor that regulation in ways provided for in the legislation.

Advantages of this approach would be:

- **Effectiveness of Ensuring Wagering Integrity.** States would retain their traditional authority of regulation of gaming, but within a framework that would still feature uniformity on matters such as licensing, and audit and accounting rules. Moreover, the ability of a state to tailor its gambling laws respects the different values states attach to gambling and eschews a “one size fits all” approach.
- **Effectiveness of Ensuring Sports Integrity.** The threats to sports integrity have a genesis in international commerce and need to be
addressed through both national and international efforts.

Having a central agency as the point of contact for intelligence is important and will facilitate creating the national and global expertise necessary to investigate and prosecute threats to sports integrity. A small state regulatory agency would not have the experience, knowledge base, information, or jurisdiction to investigate and prosecute international sports corruption. For example, it would have been difficult or impossible for state agencies to develop the case involving the FIFA bribery charges. It took the resources and expertise of the FBI and federal prosecutors to handle this.

Uniform standards defining permissible conduct, such as insider trading rules, are important to sports integrity. If states have different rules regarding what is permissible, persons wanting to skirt more restrictive regulations need only find the state with the lowest standards. This will frustrate national efforts to police sports integrity.

- **Speed to Market.** No significant federal bureaucracy would need to be created. The entity to which states would certify compliance could have a smaller footprint within an existing federal agency.

Drawbacks to this modified approach might include:
- **Effectiveness of Ensuring Wagering Integrity.** The federal body with responsibility for ensuring state compliance would have to develop expertise on how different states wanted to adjust gambling laws in their states according to local preference. This would create a federal bureaucracy without the benefits of uniformity on matters such as permitted bet types.
- **Barriers to Entry.** The economies achieved by a national uniform system of licensing and regulation would be lost, thus increasing costs to operating companies.
- **Political Viability.** This approach would certainly be more acceptable to states than a system that displaces their regulation with a federal system. But a model like this still requires federal legislation, a daunting prospect given the current political climate.

V. **ISSUES THAT WOULD NEED TO BE ADDRESSED IN ANY MODEL OF REGULATION**

Some issues would in varying degrees require the attention of policymakers regardless of the model that is implemented. A few of these issues are noted.

A. **Would the Consent of the Leagues Need to be Obtained for Their Games to be Offered for Wagering?**

One of the biggest stumbling blocks to the expansion of sports betting
beyond Nevada has been the opposition of the major sports leagues. The opposition has persisted even as the major sports leagues have given support to, and have had relationships with, fantasy sports operators whose daily games have some of the characteristics of sports betting.

The hostility toward sports betting appeared to weaken in 2014 when NBA Commissioner Adam Silver wrote an op-ed piece in the New York Times suggesting that sports betting needed to “be brought out of the underground and into the sunlight where it can be appropriately monitored and regulated.” Despite this sentiment, the NBA continued to challenge New Jersey’s plan to offer regulated sports betting and did not offer a proposal to change PASPA. More recently, Silver said he thought the laws on sports betting would be changing “in the next few years in the United States.”

After the Supreme Court accepted review of the New Jersey case in June of 2017, Major League Baseball Commissioner Rob Manfred seemed to acknowledge the coming of sports betting. He told the Baseball Writers’ Association of America, that, “[i]f there’s going to be a change in the regulatory structure . . . we needed to be in a position to meaningfully engage and shape, try to shape what the new regulatory scheme looks like.” This comment came after Manfred had earlier commented that baseball was “reexamining [its] stance on gambling.”

Although NHL Commissioner Gary Bettman curiously asserted that the

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59 Numerous teams in the major sports in the U.S. have partnership and sponsorship agreements with the daily fantasy sports companies DraftKings and FanDuel. See Gouker, supra note 27 (providing a complete list of such arrangements).

60 Silver, supra note 52.


“game doesn’t lend itself to gambling in the way football and basketball do,”\(^64\) the presence of a new NHL franchise in Las Vegas would likely dilute whatever opposition that league has.\(^65\)

It has been the intransigence of the NFL that has seemed to be the biggest obstacle to sports betting. Commissioner Goodell has been steadfast in expressing opposition to expanded sports betting. This is usually couched in terms of concerns regarding game integrity. Even Goodell, however, has acknowledged the moving of the Oakland Raiders to Las Vegas raises issues about continued opposition to sports betting.\(^66\)

A theme expressed by both Commissioners Silver and Manfred is that sports betting increased fan engagement with the sport. This is no doubt the case with the NFL (and NHL) as well. The term “fan engagement” is a euphemism for increased revenue for the leagues.

Ultimately, if a federal system of sports betting were established, the legislation would likely not allow the leagues to withhold consent for their games to be the object of wagers. On the other hand, if the system of sports betting is state-based, this option would seem to be available. However, this presents a problem.

One of the criticisms of the manner in which the leagues have opposed sports betting while supporting daily fantasy sports is that the leagues are picking the forms of sports betting that they gain from financially while opposing those they do not.\(^67\) Leagues would be vulnerable to the same criticism if they could selectively withhold consent for sportsbooks to offer their games to the public. Ultimately, the legislation establishing a sports betting regulatory regime would need to spell this out explicitly.


B. Would Sports Betting be “Monetized” for the Leagues?

From the perspective of the major sports leagues in the U.S., the opposition to expand regulated gambling may relate to one fundamental question: What is in it for us? The path forward for legalized sports betting in some respects depends upon the support or at least acquiescence of the leagues. For this support to be gained, a means of compensating the leagues for the use of their games as the source of betting may need to be established. Nevertheless, proposals requiring sportsbooks to share revenue with the sports leagues have been very controversial.

Three reasons support compensating the leagues. First, the teams and contestants have rights in their names and performance, and the sports betting operations are using this information for commercial advantage. Under existing law, the sports betting operations do not have to pay to use the names or performance data because the First Amendment preempts these rights and other intellectual property protections do not attach to the information. Despite not having a legal right to compensation, public policies underlying the right of publicity suggest that compensation to the teams and players that create the opportunity for commercial exploitation of the games for wagering may be worthy of consideration. As some commentators have noted, “Without these events, betting providers would not be able to sell a marketable product. Betting providers share this dependence on the platform sport with other stakeholders of football institutions.”


69 In National Football League v. Governor of Delaware, 435 F. Supp. 1372 (D. Del. 1977), the court found that once the NFL disseminates schedules and scores, it no longer expects generating revenue. The value of a sporting event is based on the uncertainty of the outcome. Walter Neale, The Peculiar Economics of Professional Sport, 78 Q.J. OF ECON., 1–14 (1964). So, once the event has occurred, the value of the recording of that event drops to virtually nothing. Stefan Szymanski, The Assessment: The Economics of Sport, 19 OXFORD REV. OF ECON. POL’Y 467-77 (2003). The same is true of sports wagers where the principal concerns of the player are that the games are honest (not fixed), fair (that they are played according to transparent and evenly informed rules) and they will get paid if they win. In National Basketball Association v. Motorola, 105 F.3d 841 (2d Cir. 1997) the Second Circuit found that basketball games are not subject to copyright protection because they are not original works of authorship. See Anastasios Kaburakis, Ryan M. Rodenberg, & John T. Holden, Inevitable: Sports Gambling, State Regulation, and the Pursuit of Revenue, 5 HARVARD BUS. L. REV. 27 (2015), http://www.hblr.org/wp-content/uploads/2015/01/Kaburakis-Rodenberg-Holden-Inevitable.pdf; see also C.B.C. Distribution and Marketing, Inc. v. Major League Baseball, 505 F.3d 818 (8th Cir. 2007)

Second, the sportsbooks need the efforts and cooperation of the sports governing bodies and the athletes to assure that the wagering propositions they offer are resolved based on honest competition. Giving the governing bodies a financial stake in the revenues from wagering on their sports can only enhance this cooperation.

Finally, any failures of the wagering and sports industries to assure the integrity of the game has negative economic consequences to society. Compensating the sports governing bodies to put into place additional structures and procedures can help to reduce the likelihood of these failures.

In 2018, Indiana considered a proposal for sports betting that included a one percent “integrity tax” being imposed on the handle that would go to the leagues. Some estimates are that leagues could gain as much as $2 billion/year if such a tax were imposed on a national basis. Criticisms of an “integrity tax” emphasize that a tax on handle cuts already thin margins for regulated sportsbooks by approximately twenty percent and that it is uncertain why leagues would have such high costs for monitoring integrity in a regulated market.

Another model for revenue sharing would be to impose a one percent tax on handle, with half being distributed to the leagues and players’ associations, and half to a federally administered fund that would compensate amateur and professional athletes for catastrophic injury. This type of approach would serve two functions: first, it would likely provide the leagues considerable fresh revenue. Most of the betting is currently occurring illegally with the leagues gaining nothing. The betting tax revenues come at the expense of no other lawful activity. The other benefit to this approach is that it would allow the leagues to present themselves as advancing a good cause. For example, it would offer the NFL the opportunity to support sports betting as a way of advancing societal interests and holding itself out as a good public citizen. Providing compensation to injured athletes might help assuage concerns about the safety of contact sports like football.

Without question, the formula for establishing such a system would be problematic and likely contentious. Administrative costs relating to collecting the tax and distributing the proceeds might be significant. Nevertheless, if

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72 Id.


leagues were ready to put their weight behind broadly legal sports betting contingent on this being worked out, there would be incentives for all interested parties to reach an agreement.\footnote{See David Lariviere, Legalization of Sports Betting Would Be Huge Revenue Producer for Leagues, Expert Says, FORBES (Sept. 19, 2014, 11:13 AM), https://www.forbes.com/sites/davidlariviere/2014/09/19/legalization-of-sports-betting-would-be-huge-revenue-producer-for-leagues-expert-says/#551040b02d1c.}

On the other hand, sportsbooks have a compelling argument that the margins on sports wagers are so small that any revenue sharing would raise prices and drive consumers to illegal markets where they can get better odds. Moreover, the concept of revenue sharing is contrary to existing law in the United States where the sportsbooks only need the results of the contest or events within the game (i.e., names, statistics, scores, real-time data) and anyone can use them for free once made public.\footnote{Dietl, Betting Scandals, supra note 70.} Therefore, the government should not create rights not recognized by law to benefit an industry.

A potential solution that would direct revenue to the leagues while not imposing new taxes on sportsbooks involves the existing federal excise tax on sports wagers. This tax on sports wagers was first imposed in 1951 at a rate of ten percent on the gross handle.\footnote{DAVID G. SCHWARTZ, CUTTING THE WIRE: GAMING PROHIBITION AND THE INTERNET 169 (2005).} The legislative history of the law creating the tax was to “facilitate the enforcement of state criminal laws against gambling.”\footnote{Note, The Federal Gambling Tax and the Constitution, 43 J. OF CRIM. L. AND CRIMINOLOGY 637, 637 (1953).} If the purpose of the tax was to prevent legitimate, licensed sportsbook operations from operating, it succeeded, as no sportsbook could operate profitably with that tax load.

In 1974, the tax rate was reduced to a more manageable two percent with the result being that the first casino based sportsbooks sprang up in Las Vegas. And in 1983, the tax was reduced to its present rate of 0.25%.\footnote{Schwartz, supra note 77, at 169.}

Based on figures compiled by the Urban Institute & Brookings Institution Tax Policy Center, approximately $4.2 million in revenue was generated by the sports wagering excise tax in 2015, as compared to the $3.3 trillion of total tax revenue collected by the IRS.\footnote{Urban Institute & Brookings Institution Tax Policy Center, Federal Excise Tax Revenue (2015), http://www.taxpolicycenter.org/statistics/federal-excise-tax-revenue.} However, if sports betting were more widely available, the excise tax revenues could increase dramatically. A total handle of $100 billion in regulated US markets would produce $250 million in excise taxes.

While the federal government might be unwilling to forego all that revenue, there is a federal interest in reducing corruption in sports wagering.
Directing some of the excise tax revenue to the sports governing bodies can help to curb corruption while still allowing for sportsbooks to be profitable undertakings. This approach has the benefit of not imposing additional costs on sportsbooks which are already paying the excise tax. The excise tax on sports betting was created to discourage betting on sports, a sentiment that has changed considerably over the years. Ultimately, if a system of sports betting with integrity is to exist in the U.S., compromises from all parties, including the federal government, will be needed.

As sports betting markets mature and introduce more betting products, opportunities for monetizing the betting activity to benefit the leagues will increase. For example, sports betting could include betting exchanges where bettors offer or take positions on sports events. This peer-to-peer model allows buyers and sellers to be matched up on opposite sides of betting propositions. The betting platform operates similar to a stock exchange, charging a commission fee on the transactions conducted. Exchange wagering platforms in the U.S. originated in horse racing, with New Jersey one of the first states to authorize such markets.81

To a significant extent, the exchange wagering model of sports betting resembles traditional securities markets. The federal government predominantly regulates these financial markets.82 This may be a factor that would tilt the preferred regulatory model for sports betting exchanges toward a federal rather than state orientation. The diversity of betting offerings in exchange wagering may also be attractive to the sports leagues because the market offerings would not necessarily be tied to point spreads. However, the leagues could still profit from the betting exchanges through a surcharge on the transactions processed through the exchange. This is an approach used in other countries where sports

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81 Pioneered by Paddy Power Betfair, and now the world’s largest publicly traded online gambling company, exchange wagering is a high-tech manner of gaming aimed at enticing younger gamblers into the market. The European company is hoping to use the internet to tap into the $3.5 billion wagered on horse racing online in 2015. See Joe Drape, High-Tech Wagering Sees Gateway Into America: The Horse Track, N.Y. Times (July 29, 2016), https://www.nytimes.com/2016/07/30/sports/horse-racing/betfair-exchange-wagering-gambling-horse-racing.html.

82 Equities regulation falls within the purview of numerous organizations. Federal government regulation is undertaken by the Securities and Exchange Commission’s Division of Trading and Markets. Among their responsibilities is to “regulate[] the major securities market participants, including broker-dealers, self-regulatory organizations...and transfer agents.” Trading and Markets, U.S. SEC. & EXCHANGE COMM’N, https://www.sec.gov/page/tmsectionlanding (last modified Jan. 30, 2017). The Financial Industry Regulatory Authority (FINRA) is a non-profit organization authorized by the federal government to regulate equities markets. FINRA regulates the markets by writing and enforcing rules for brokers, examining firms for compliance with rules, and encouraging transparency. See About FINRA, FIN. INDUSTRY REG. AUTHORITY, https://www.finra.org/about (last visited Mar. 13, 2018). Other regulatory activities in the equities market are undertaken by the individual stock exchanges, such as the New York Stock Exchange.
betting is widely permitted.

CONCLUSION

The court challenges to PASPA have been a compelling part of the story of the ascendance of sports wagering in the U.S. But as is often said, the devil is in the details. It would be unfortunate if the expansion of sports betting in the U.S. were threatened or stunted because of regulatory failings that undermined the integrity of the activity. Careful thought needs to be given to the many issues raised here, or the long legal battle to bring sports wagering out of the shadows and into the light of regulation might be in vain.