



Future of Fantasy Sports: Understanding Regulatory, Political Issues



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Welcome to the Panel

- Daily Fantasy Sports has emerged as one of the more intriguing entertainment activities with the support of the major sports leagues and financial sponsors

Our Panelists for Today's Webinar



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A Brief History – The Genesis of DFS

- Season-long fantasy is presumed to have begun in 1963 when the National Baseball Seminar was introduced
- President George W Bush signed the Unlawful Internet Gaming Enforcement Act (“UIGEA”) into law in October 2006
- The law provides an exemption from its prohibitions on fund transfers for “participation in any fantasy or simulation sports game or education game or contest” that meet certain criteria:
 - Prizes are pre-determined and can’t be altered based on the number of participants
 - Outcome is based predominantly on skill
 - Not based on a single performance of an individual athlete in a single sporting event
 - No winning outcome may be based on the score, point spread or performance of any single team
- UIGEA does not provide a blanket exemption; state law supersedes
- The first DFS sites sprung from a legal interpretation of UIGEA
- SGC believes Fantasy Sports Live, launched in June 2007, is the first DFS site
 - FanDuel – 2009
 - DraftKings – 2012

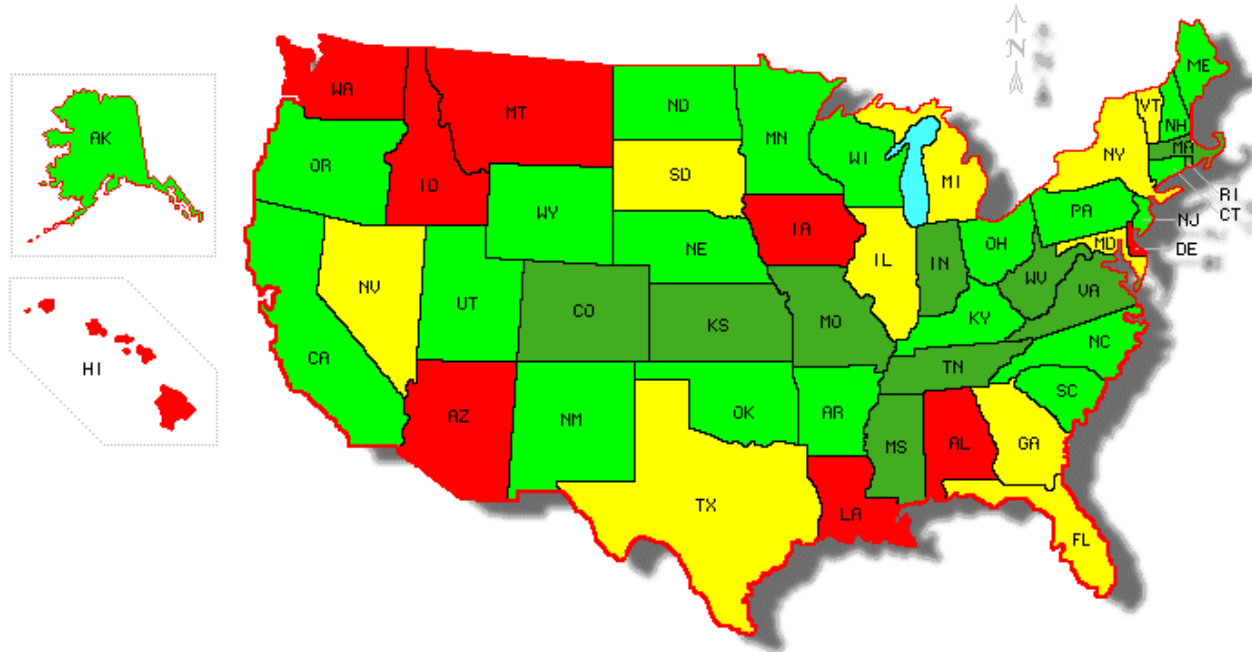
Comes Under Legal Scrutiny

- On September 27, 2015 a DraftKings employee accidentally releases ownership data before lineups locked
 - The same DraftKings employee subsequently wins \$350K on FanDuel
- Lawsuits – 25 and growing
- Increased state and federal scrutiny
 - Federal
 - May 2016 hearing of the House Energy and Commerce Committee
 - A federal grand jury in Tampa is investigating DFS
 - The New York federal prosecutor, Preet Bharara is investigating the DFS business model
 - States
 - The Attorneys General of twelve states issued opinions that DFS violates state law
 - Including the Attorney General of NY where the legislature passed legislation legalizing DFS in June 2016
 - Nevada Gaming Control Board: can operate if licensed
 - Michigan Gaming Control Board: DFS is illegal

Bottom Line – Know Which States are Considered Legal

SGC considers DFS legal, or operational, in 31 states with 58% of the total US population. New York passed DFS legislation but the Governor has not yet signed it.

- - Legal
- - Operational
- - Challenged
- - Banned



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Eleven States Have Declared DFS Legal in that State's Borders

In total, eight legislatures have passed legislation authorizing DFS, while the AGs in Massachusetts, West Virginia and Rhode Island have issued opinions that DFS does not violate state law

State	Population	Date Passed	GGR tax rate	Annual license fee	Minimum age	Limit entries	Identify highly skilled players	Regulator	Interstate play	Amateur sports
New York	19,795,791	6/16	15%	NA	18	Yes	Yes	New York State Gaming Commission	Yes	Prohibited
Virginia	8,382,993	2/16	NA	\$50,000	18	Yes	NA	Department of Agriculture and Consumer Services	Yes	NA
Massachusetts	6,794,422	NA	NA	NA	21	Yes	Yes	Attorney Generals Office	NA	Prohibited
Indiana	6,619,680	3/16	NA	\$50,000/\$5,000 annual renewal	18	Yes	NA	Indiana Gaming Commission	NA	Prohibited
Tennessee	6,600,299	4/16	6%	NA	18	Yes	Yes	Secretary of State	NA	NA
Missouri	6,083,672	5/16	11.50%	Lesser of 10% or \$10,000	21	NA	Yes	Missouri Gaming Commission	Yes	Prohibited
Colorado	5,456,574	5/16	(1)	(1)	18	Yes	(1)	Division of Professions and Occupations	(1)	Prohibited
Mississippi	2,992,333	4/16	(2)	(2)	18	(2)	(2)	(2)	(2)	(2)
Kansas	2,911,641	5/15	NA	NA	NA	NA	NA	NA	NA	NA

1) The Colorado legislation left the promulgation of regulations, taxes and fees to the Division of Professions and Occupations
 2) The Mississippi legislation creates the Fantasy Sports Task Force to promulgate regulations by October 15, 2016

Source: Spectrum Gaming Capital

Twenty-one other states are considered operational because almost all sites are in operation in the state and the state has not articulated a position on DFS.



Does Legislation Make it Legal?

- State Level
 - State prohibition on gaming or gaming expansion
 - Pair with iGaming legislation
- Federal
 - Professional and Amateur Sports Protection Act (“PASPA”)
 - Interstate Wire Act
- Potential plaintiffs in a court challenge
 - Casino operators
 - Native American Tribes
 - Professional and amateur sports leagues

DFS Operators Offer a Variety of Sports

As the states that legalized DFS start to put the regulations into practice, this list of sports will likely change as many states prohibit contests on amateur sports

Site	Founded	Sports offered										Types of Contests		
		NFL	MLB	NBA	NHL	MMA	Golf	Soccer	Nascar	eSports	Daily	Season	H2H	
DraftKings	2012	X	X	X	X	X	X	X	X	X	X	X		X
FanDuel	2009	X	X	X	X						X	X		X
Draft Ops		X	X	X	X	X						X		X
Draft	2015	X												X
StarsDraft (Amaya Gaming)	2014	X	X		X			X				X		
Star Fantasy Leagues	2012	X	X	X	X							X	X	
Kountermove	2010					X						X		
Draft Day (Sportech)	2011	X	X	X	X			X				X		
Fantasy Aces	2013	X	X	X	X			X				X		X
FantasyDraft	2014	X	X	X	X			X				X	X	X
Fantasy Feud	2011	X	X	X	X			X		X		X	X	X
Boom Shakalaka	2014	X	X									X		X
DraftPot	2014	X	X	X	X			X		X	X	X		
Head2Head Sports (Sports Information Group)	1994	X	X	X	X			X		X		X		X
SportsLock	2011	X		X										
Smash Mouth Fantasy	2014	X	X	X								X	X	X
Swoopt (theScore)	2011	X	X	X	X							X		

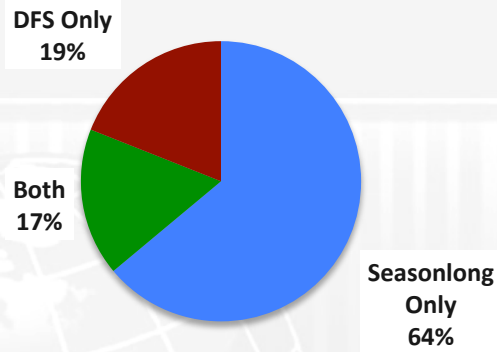
Source: Spectrum Gaming Capital, company websites



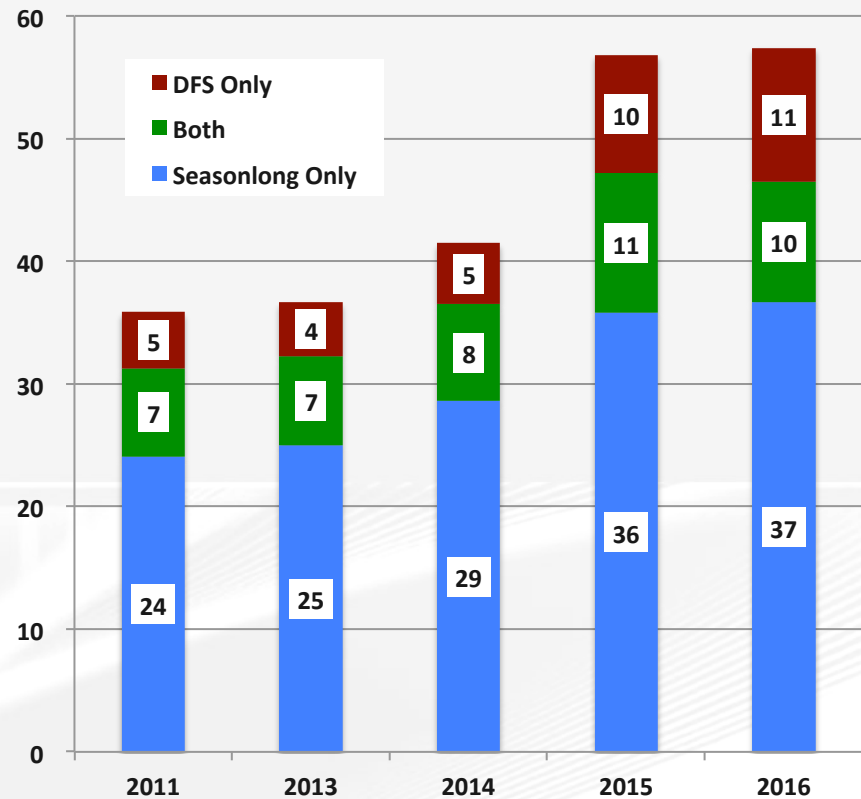
Daily Fantasy Sports has been the Primary Driver of Fantasy Sports Participation

- Approximately 36% of fantasy sports players play DFS
- Since 2011, the number of participants who claim to play DFS only has grown 137% to 11 million people
- During that same time period, the number of participants who claim to play season-long only has grown 52% to 37 million

Breakdown of Participation by Activity



Growth In Fantasy Sports Participation



Source: Fantasy Sports Trade Association

Less than 10% of Americans Participate in DFS

Calculation of DFS Participation Rate

Population of U.S	319
Less: Population under 18	74
Less: 18+ population of WA, LA, IA, MT,AZ	17
US population eligible to play DFS	228
Seasonlong fantasy sports participants	37
DFS only participant	11
Participants of seasonlong and DFS	10
Participation Rate	
Seasonlong fantasy sports participants	16%
DFS only participant	5%
Participants of seasonlong and DFS	4%

Source: US Census Bureau, Fantasy Sports Trade Associate, SGC

- The 21 million participants in DFS are estimated to have paid \$2.9 billion in entry fees
 - SGC estimates this translated into approximately \$245 to \$260 million in revenue
- As such, each DFS participant average \$140 in contest entry fees annually
- To put the \$2.9 billion into context, Nevada sports books accepted over \$4.5 billion in wagers over the LTM ended May 2016
- The participation rate could grow as:
 - More states legalize DFS
 - Legislation legitimizes the business model in the eyes of many consumers

Explaining the Business Model

Contest participation	100%	93%	85%
Number of positions in contest	10,000	10,000	10,000
Entry fee	\$5	\$5	\$5
Actual participants	10,000	9,300	8,500
Entry fees	\$50,000	\$46,500	\$42,500
Prize payouts	45,000	45,000	45,000
Revenue	\$5,000	\$1,500	(\$2,500)

Overlay Explained

- When a DFS contest has negative revenue it is called overlay
- Occasionally overlay is done purposely because large prize pools generate excitement, word-of-mouth advertising and new player signups
- The DFS player likes overlay because it improves the odds of winning prize money

- The mechanics of daily fantasy are similar to pari-mutuel wagering
- Players pay an entry fee to enter individual contests
- The DFS site takes a fee, or rake, of entry fees
 - Typically 10%
 - As such, DFS operator takes no risk on contests
- The primary difference between pari-mutuel and DFS
 - In pari-mutuel wagering, the payout rises as more people wager
 - In the definition of fantasy sports from UIGEA, the prizes are pre-determined and can't be altered based on the number of participants
 - As such, industry revenue can be less than 10% of entry fees and individual contests can generate negative revenue

Avoid the Mistakes Other States Have Made

In our view, the first states to pass legislation made two crucial errors that can impact the future of the industry

- **Annual license fees will stifle competition**

- Virginia, Indiana and Missouri charge an initial, or annual, license fee
- In Missouri, the annual fee is the lesser of \$10,000 or 10% of the prior year revenue
 - For smaller DFS operators this can result in a 22.5% tax rate
- In Virginia, the annual fee is \$50,000 and it is believed that the smaller DFS sites will not participate in Virginia

- **Rethink the tax paradigm**

- In the gaming industry, the tax regime is based on gross gaming revenue
- Because of overlay, it is possible that there will be no tax, or potentially a refund, or individual contests
- A smaller rate on entry fees will maximize revenue to the state