

**WRITTEN TESTIMONY OF  
THE SMALL BUSINESSES OF FANTASY SPORTS TRADE ASSOCIATION  
PRESENTED BY ALEX KAGANOVSKY BEFORE  
THE PENNSYLVANIA HOUSE  
GAMING OVERSIGHT COMMITTEE  
TUESDAY SEPTEMBER 27, 2016**

Good morning Chairman Payne and members of the House Gaming Oversight Committee.

My name is Alex Kaganovsky. I am the Co-Founder of The Small Businesses of Fantasy Sports Trade Association. I come before you today to discuss decisions made by your counterparts in other states as they pertain to fantasy sports legislation.

It is my hope that Pennsylvania will not make the same mistakes that the majority of states have made on this issue.

Small businesses of all kinds are fragile. The increases in cost, through taxes and fees, or through regulatory burden, can take a profitable business into bankruptcy with the stroke of a pen. Small fantasy sports businesses are no different.

What we have experienced in 2016 is crushing. Of the eight states that have passed fantasy sports legislation this year, only one – Colorado – does no harm to small businesses. New York is OK, but not good, and the remainder are cost prohibitive for small companies. We are financially locked out of those states because legislatures do not understand the impact of their actions on small businesses.

I will stress in my comments today that we are NOT DraftKings or FanDuel. We are little mom and pop entrepreneurial business trying to make our dreams of owning a small business a reality.

In their zeal to regulate the two giant companies – who control more than 90% of the marketplace – legislatures are crushing small businesses. Please, Please, Please do not follow their lead. My request of you here today is that you do no harm. Regulation need not be prohibitive to the conduct of business. Consumer protection is possible without pushing small companies out of the marketplace.

My company, the Fantasy Football Players Championship, offers a variety of paid entry, season-long contests. We are in our ninth year of operation and we have a growing company. The vast majority of companies in this space are like ours. We are self-financed entrepreneurs that offer season-long contests to football fans. We are not DraftKings. We are not FanDuel. We are not venture capitol backed businesses formed to make billions of dollars.

The irony of this entire situation is that season-long fantasy sports contests have been in existence for three decades. They have been online in some form or another for two decades. There has been significant growth in the industry since the United States Congress passed the Unlawful Internet Gambling Enforcement Act that exempted online fantasy sports contests from online gambling prohibitions. The United States government gave a green light to fantasy sports companies to operate online businesses offering fantasy sports contests as long as they did not violate state law in doing so.

DraftKings and FanDuel changed all of that with their massive advertising spend in 2015. Their advertising theme was reminiscent to a get rich quick scheme intended to convince average Joes that they could strike it rich in daily fantasy sports. Fantasy sports has never been about getting rich quick. It has always been a hobby for sports fans that want to test their knowledge and team management skills against those of other sports fans.

The 2015 ad spend by DraftKings and FanDuel did two things. It mischaracterized traditional fantasy sports as something that it had never been – instant games offering daily or weekly jackpots of millions of dollars. And, it characterized all fantasy sports companies as giant corporations in need of state regulation.

Because of this massive ad spend, legislatures across the country felt the need to react swiftly to the evolving situation. And in their effort to “do something” about

DraftKings and FanDuel, they are crushing small businesses that are nothing like DraftKings and FanDuel.

Of the eight states that have passed fantasy sports legislation in 2016, only one has done no harm to small companies. Colorado got it right. They understood that giant companies offering daily games are different than tiny companies. They understood that regulation, while important, can crush the life out of small businesses. So, what did Colorado do to get it right? They differentiated large businesses from small businesses by placing a player threshold in their law that has those companies with over 7500 players being licensed and taxed, and those companies with 7500 or fewer players registering with the state, but without paying taxes and fees and without the expensive regulatory costs.

The first two states to pass fantasy sports laws in 2016, Virginia and Indiana, couldn't have gotten it more wrong for small businesses. They set the cost of entry for all companies at \$50,000. If a company wants to offer its fantasy sports contests to sports fans in either of those two states they have to pay a fee of \$50,000 to do so. What they failed to realize is that no small companies make \$50,000 profit in either Virginia or Indiana, so, ironically, in their effort to regulate the industry in response to the DraftKing and FanDuel ad spend, they gave the entire state to those two companies and forced everyone else out.

Tennessee passed a law that recognized that a percentage based tax structure and a graduated fee structure was more fair to small business than the very high flat fee in

Indiana and Virginia. But, Tennessee got it wrong by adding massive regulatory costs to their law that has kept all but four companies out of that state. The Tennessee tax is set at a flat 6% of net revenues and the fee structure is graduated based on net revenue, but the regulatory costs of annual audits and bonding to cover contest winnings for players has priced most companies out of Tennessee.

Unfortunately, Missouri got it really wrong when they followed Tennessee's lead on costly regulatory issues and compounded that harm by charging small companies 10% of their net revenues as an annual application fee and another 11.5% of their net revenues as an annual operation fee. No small companies can afford to operate in Missouri. Another state where the two giant companies will have a duopoly in the marketplace and small companies are forced out.

Mississippi passed a law that calls for a study of the industry and for a report to be published next month, and while it was reported that all companies could operate in the interim, the cost of their regulatory requirements have kept most companies out of that state. We are hopeful that the Mississippi legislature will realize that small companies are not DraftKings and FanDuel and that they need to keep taxes and fees and the cost of regulatory compliance low if they want to meet the needs of fantasy sports fans in their state.

Massachusetts has passed a law that is in effect until July 31, 2018 that basically requires companies to follow the administrative rules put in place by their attorney

general. The cost of regulatory compliance will keep most small companies out of Massachusetts.

Here in Pennsylvania there are two concepts that seem to be in discussion. One concept is similar to the Tennessee model with a relatively low tax, but with very high regulatory compliance costs. The other concept proposes a higher tax, but contains an opportunity for small companies to participate by placing a threshold under which small companies can operate here without all of the regulatory compliance costs. It is our hope that the General Assembly will pursue the concept with a reasonable tax structure and low regulatory compliance costs for small companies.

In closing, I think it is important that you understand two very important observations regarding fantasy sports. First, two large companies make up 90% of the fantasy sports market in terms of revenues generated. Second, fantasy sports is separated about evenly in terms of the number of players between the daily offerings of DraftKings and FanDuel and season-long companies like mine. When finalizing your law please keep these issues in mind. One size does not fit all in fantasy sports and season-long and daily fantasy sports are very different and need separate consideration.

## 2016 Fantasy Sports Laws

- Virginia
  - <http://law.lis.virginia.gov/vacodefull/title59.1/chapter51/>
  - <http://www.vdacs.virginia.gov/pdf/fcregistrationform.pdf>
  - \$50,000 application fee too costly for small companies
  - Regulatory burden too costly for small companies
    - Annual audits
    - Annual game testing
    - Reserve bonding
  - Only 4 applicants to date – No Season-long companies
    - DraftKings, FanDuel, Fantasy Draft, Eagle Strike (kiosks).
    - <http://www.vdacs.virginia.gov/pdf/registeredfcooperators.pdf>
- Indiana
  - [http://www.in.gov/igc/files/PFS\\_SB\\_339\\_Fantasy\\_Sports.pdf](http://www.in.gov/igc/files/PFS_SB_339_Fantasy_Sports.pdf)
  - Notice of Intent to File Application
    - <http://www.in.gov/igc/2819.htm>
    - 14 companies filed intent letters, does not mean they will apply.
  - Draft Application
    - [http://www.in.gov/igc/files/PFS\\_Application\\_07\\_06\\_16\\_.pdf](http://www.in.gov/igc/files/PFS_Application_07_06_16_.pdf)
    - Operator applications due November 1, 2016
  - \$50,000 application fee too costly for small companies
  - Regulatory burden too costly for small companies
- Massachusetts
  - Allows operators to offer fantasy sports contests until July 31, 2018 as long as they follow the Attorney General rules.
  - AG rules focus on “daily fantasy sports” and cost of regulatory compliance is very high.
- Tennessee
  - Application form
    - <http://sos-tn-gov-files.s3.amazonaws.com/forms/ss-6800.pdf>
  - Application fee could be as much as 25% of previous year’s net revenue for small companies, and as little as 2.5% for large companies.
  - Rules and Regulations
    - <http://share.tn.gov/sos/rules/1360/1360-03/1360-03-05.20160629.pdf>
  - 6 Companies applied, only two have been licensed
    - Fantasy Draft
    - Sportshub
    - Draft
    - Draftboard
    - FanDuel (licensed)
    - DraftKings (licensed)
  - 6% tax
    - Reasonable tax rate

- Regulatory burden too costly for small companies
    - Annual audit
    - Reserve requirements too costly
    - Prohibition on "auto draft"
- Mississippi
  - Created a task force to study fantasy sports and issue a report for future legislation. Report is due October 16<sup>th</sup>.
  - Regulatory burden too costly for small companies
    - Annual audits
    - Reserve bonding
- Colorado
  - Differentiates large companies from small companies by creating different requirements for companies with 7500 players or less.
  - Small fantasy contest operators must register by July 1<sup>st</sup>, 2017.
  - Large companies must be licensed by July 1<sup>st</sup>, 2017.
  - Small companies exempt from annual audit requirements.
- Missouri
  - 10% annual application fee
  - 11.5% annual operation fee
  - Regulatory burden too costly for small companies
    - Annual audits
    - Reserve Bonding
- New York
  - 15.5% tax/fee
    - High, but not highest
  - Application for Temporary Permit
    - <https://gaming.ny.gov/ifs/Application%20for%20temporary%20registration.pdf>
    - Extremely difficult application and process
  - 9 Temporary Permits Granted
    - <https://gaming.ny.gov/ifs/>
      - DraftKings
      - FanDuel
      - Yahoo
      - Fantasy Draft
      - Draft
      - iTeam Network
      - DraftDay
      - Synkt Games, Inc. d/b/a letsRUMBL
      - Fantasy Aces LP
  - Regulatory burden less onerous than other states
- Pennsylvania HB2150 Dunbar
  - As amended by Rep. Youngblood--A8734



- 5% fantasy contest tax
- Up to 5% application fee
- Annual audits and annual game testing – very expensive
- Bonding for reserve requirement is very expensive
  
- Pennsylvania SB1324 Williams
  - Application fee not to exceed 5%
  - 12% tax
  - Small season-long fantasy companies exempt from the annual audit and game testing requirements unless the gaming commission requires otherwise.
  - Third party escrow requirement replaces reserve requirements for small season-long companies.