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Research Brief: SCOTUS Repeal of PASPA

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Earlier today, the U.S. Supreme Court issued a ruling on the constitutionality of the Professional and Amateur Sports Protection Act of 1992 (“PASPA”) in the *Murphy v. NCAA* case overturning the law and allowing sports betting to move forward in the United States. In a 7-2 decision, the Supreme Court also provided a victory for states’ rights. Today’s ruling allows commercial entities in states and Native American tribes to move forward to conduct sports wagering.

The *Murphy v. NCAA* case was heard by the Court in December. At the time, Global Market Advisors (GMA) had predicted that the court would rule in favor of states’ rights and sports betting on a 6 – 3 vote supporting New Jersey’s argument. The opinion of the Court issued today was led by Justice Samuel Alito and supported by Chief Justice John Roberts and Justices Stephen Breyer, Neil Gorsuch, Elena Kagan, and Anthony Kennedy. Justice Clarence Thomas wrote a concurring opinion. The dissenting opinion was issued by Justices Ruth Bader Ginsburg and Sonia Sotomayor. Justice Breyer joined the dissenting opinion on a small portion of the overall opinion from the court.

Prior to the opinion issued today, GMA has released a series of information pieces on sports betting including a white paper titled, “[An Examination of Sports Betting in America & Forecast of Revenues by State](#)” highlighting the opportunity as well as a research briefing discussing the “[Economics of Sports Betting.](#)” GMA estimates that total state revenue for sports betting is between \$1.8 billion to \$9.0 billion depending on the regulatory structure, tax rate, and which states would opt-in with the repeal of PASPA. However, the paper notes that for the market to succeed, it must be regulated and taxed properly while addressing illegal sports betting.

NEXT STEPS

Prior to the repeal of PASPA, only four states (Nevada, Oregon, Montana, and Delaware) allowed some form of sports betting. They were all grandfathered in prior to the passage of PASPA in 1992, with Nevada being the only state that has offered full sports wagering. Almost two dozen states either have explored or continue to explore their options regarding the regulation of sports betting.

LAS VEGAS

7220 S. Cimarron Rd
Suite 220
Las Vegas, NV 89113
United States of America
+1 (702) 547-2225

BANGKOK

199 Column Tower G
24th Floor, Suite 2405
Kweng Kongtoey, Khet Kongtoey
Bangkok, Thailand 10110
+66 (0) 6 1664 0059

TAIPEI

Suite 216, 2F
#97 Dunhua S. Road
Sec 2
Taipei, Taiwan
+886 936 106 737

DENVER

757 E. 20th Ave
Suite 370 #406
Denver, CO 80205
United States of America
+1 (303) 759-5944

www.globalmarketadvisors.com

There are two states that recently expanded sports betting in anticipation of the repeal. This includes Pennsylvania which legalized it in 2017, and West Virginia which legalized it earlier this year. Both states prove to be interesting dynamics as they move forward in implementing sports betting. Pennsylvania has a 36 percent tax rate, which makes sports betting almost ill-conceived to operate within the borders of the Commonwealth. If Pennsylvania is to be successful in its sports betting endeavors, the state must go back and modify the act with a lower tax rate that takes the economics of sports betting into consideration.

West Virginia has recently been in the news as the governor last week announced that he would impose an integrity fee on any casino operating sports betting, to pay the leagues their ransom to conduct sports betting operations. While the issue will be sorted out in the coming weeks, members of the state legislature, operators, and even those citizens interested in participating in sports betting should advocate that the integrity of sports betting lies in the regulations and not in a money grab by the sports leagues. The Governor should fold on his intentions to further obstruct the operations of sports betting through this extra tax on operators for the benefit of the leagues that will already be rewarded through additional interest and viewership.

GMA believes that a handful of states will likely still move forward this year. This includes New Jersey, Delaware, Mississippi, New York, Rhode Island, Massachusetts, and Illinois. As many states have already adjourned their legislative session, the likelihood of other states joining the debate this year is limited, but more than a dozen states will likely take up the issue in 2019. Major states that may look at legislation beyond those listed above include Kentucky, Iowa, Kansas, Missouri, Louisiana, Indiana, Ohio, and Michigan. Native American Tribes will also see significant activity but may have to move forward with adjustments in their existing compacts before operations can begin. There will be significant activity across all 50 states throughout the next several years as the initial states move and the neighboring states react to the legalization of sports betting. Education will be a key during this time to understand the economics of sports betting to capture revenue to the state while tackling the illegal market that currently exists in every state.

One thing that remains in question is whether or not this may prompt federal legalization, which has been attempted in the past to regulate online gaming. Considering the current political climate in Washington, D.C., a federal framework for sports betting seems improbable in the near term, especially when considering that this current SCOTUS decision was favorable toward states' rights. There are current pressing priorities in Congress that will be taken with a higher priority.

INTEGRITY FEE

As state governments continue to contemplate how to formulate the regulatory framework for sports betting and how they can maximize the benefit to the community in terms of tax revenue and other economic impacts, they should understand the basic economics behind the industry and garner insight from existing stakeholders. On average, operators only hold approximately five percent of handle. As



such, if a market is projected to generate one dollar in handle, only five cents of that dollar is held by the operators as revenue. This small percentage is where the operator must pay for all of its operations, the cost of data from which the leagues benefit, as well as the taxes it must pay to both the state and federal governments.

Several professional sports leagues have proposed that they should receive an integrity fee (equivalent to one percent of handle) from those states that legalize sports betting. It is important to note that there is not an integrity fee paid to any league in the existing market of Nevada today. The integrity of the game is monitored by operating sports books to ensure that games are fair and held to a high standard. Nevada sports books over the years have been the first to catch any degradation of integrity that may exist in a contest(s).

While one percent of handle may seem like a marginal amount, it is the equivalent of a 20 percent tax on revenue. As a result of the push back to this money grab in some states, the leagues have backed off the full one percent and the “integrity fee” label, opting for a lesser amount and referring to it as a “royalty fee.” Based off of the current market in Nevada, the average sports book operator maintains approximately 40 percent of revenue as EBITDA. A 20 percent fee on revenue would leave the operator with only a 20 percent EBITDA margin. In states that look to raise the state tax fee higher than the current rate of 6.75 percent in Nevada, this only further erodes the ability for operators to make their sports book profitable. States with higher tax rates, such as Pennsylvania at 36 percent, make it virtually impossible to operate legal sports books, thereby allowing the illegal market to continue to flourish.

Integrity exists in the games due to proper regulation and oversight by the sports books, not by a fee paid to the sports leagues. The sports leagues will benefit from the expansion of sports betting due to the increase in viewership and interest that stems from the influx of new sports betting participants.

WIRE ACT

Even though PASPA has now been overturned, operators may still face the obstacle of conducting business through online channels due to the Federal Interstate Wire Act of 1961 (“Wire Act”). The Wire Act in itself has divided the gaming industry as stakeholders debate interpretations of the act (particularly the 2011 memo highlighting the opinion of the Attorney General’s office under the Obama Administration). The stakeholders pushing for the Restoration of America’s Wire Act will continue to advocate this issue for the foreseeable future. This may play into the potential of online gaming that exists in states like Nevada, New Jersey, and Delaware that allows them to compete amongst themselves. Pennsylvania will join that list soon as it expands into online gaming.

How the federal government will opine on an interpretation of the Wire Act remains unknown. Current Attorney General Jeff Sessions may try to produce a similar memo to the one it produced to overturn the Cole Memorandum on the legalization of marijuana issued during the Obama Administration. The decision by the Supreme Court should be viewed first and foremost as a victory for states’ rights which has been championed by the Trump Administration. It is hopeful that these activities, as currently allowed through the 2011 interpretation of the Wire Act, will be allowed to continue. Mobile wagering provides the



greatest opportunity for operators and states to recapture the illegal market while allowing convenience to the player. GMA believes that states will continue to be allowed to offer this service to customers, similar to New Jersey and Nevada.

NEVADA AS A FRAMEWORK

As states look at their own path to legalization, the State of Nevada has demonstrated a path to successful sports betting implementation through strict regulation. States should evaluate Regulation 22 of the Nevada Gaming Control Board Regulations, which solely deals with race books and sports pools, to understand the tax structure, licensing procedures, and other regulations created to bring integrity to contests.

The level of convenience of wagering that is afforded to players will be key to the success of each market. The State of Nevada offers a great example of how a state can work with operators to make the market more accessible to patrons with the advance of online, mobile, and kiosk technology. These new wagering platforms have evolved over time through the use of geo-location technology. It will be important for each jurisdiction to consider offering a multitude of wagering options to make their sports betting product more competitive with other legal and illegal offerings. Each state can utilize the State of Nevada as a guide in deciding how to allow for items such as initial registration with a physical sports betting venue.

To successfully compete against the illegal market, states will have to offer a reasonable tax regime that allows operators to have some margin of operational success. By bringing in quality operators that monitor games and contests, as the State of Nevada has done for decades, the integrity of the game can be maintained and ensured. Scandals like the point shaving contest that occurred in the 1990s at Arizona State and the referee betting scandal that occurred in the NBA in 2007 were discovered by Nevada sports books and their effective monitoring of games.

The sports leagues will benefit greatly from the expansion of sports betting due to the increase in viewership and interest that stems from the influx of new sports betting participants with PASPA now overturned. Owner of the Dallas Mavericks, Mark Cuban, has already been quoted as saying that the value of his organization just doubled overnight. With a focus and increased interest in sports betting, Cuban is absolutely correct that the leagues will benefit from this expansion. This is even more of a reason that they do not need a payout from a regulated market that brings integrity through the process and not through a fee.



CONTACT INFORMATION

Brendan Bussmann

Partner, Managing Director of Government Affairs

bdb@globalmarketadvisors.com

John English

Partner, Managing Director of Sports and Technology

jje@globalmarketadvisors.com

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