

**ESTIMATE OF FEDERAL REVENUE EFFECT OF
PROPOSAL TO
REGULATE AND TAX ONLINE GAMBLING**

EXECUTIVE SUMMARY

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UC Group

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On May 6, 2009, Rep. Barney Frank (D-MA) introduced the "Internet Gambling Regulation, Consumer Protection, and Enforcement Act" (H.R. 2267), which would provide for the licensing and regulation of lawful Internet gambling by the U.S. Department of the Treasury. Also on May 6, 2009, Rep. Jim McDermott (D-WA) introduced a companion bill, the Internet Gambling Regulation and Tax Enforcement Act of 2009 (H.R. 2268), that would impose a fee on companies licensed to provide online gambling services in the United States.

PricewaterhouseCoopers LLP ("PwC") was retained by UC Group to estimate the federal revenue effect of H.R. 2267 and H.R. 2268. UC Group is an online payment services provider that does not operate in the U.S. market. PwC has not taken any position in favor or against adoption of the legislative proposal, and has not been retained to provide any advocacy services in connection with the proposal.

The revenue analysis is based on available data, conversations with industry experts, and our professional judgment. The conclusions rely on projections of future events and behavioral responses that inherently are uncertain. The revenue analysis is intended to provide Congress with information that may be useful in the official scoring of the legislation's revenue effects.

The Frank bill would create a regulatory and licensing regime for online gambling. The McDermott bill would impose a two-percent licensing fee on deposits received by licensed operators and clarify the treatment of internet gambling under the tax code. The analysis in this report takes into account certain clarifications and modifications to the Frank bill, including the following:

1. Internet gambling licensees would be required to be incorporated in the United States, and senior management and computer equipment would be required to be located in the United States.
2. Congress would authorize states to impose indirect taxes on licensees with respect to wagers placed from within their jurisdictions, whether or not the licensee has nexus with the particular state.
3. All online wagering would be subject to the federal wagering excise tax.¹

The revenue analysis is based in part on projections by H2 Gambling Capital ("H2GC") of U.S. online gambling revenues under present law and under a legalized market. H2GC is a consulting firm that tracks online and land-based gambling on a global basis. H2GC collects data from a variety of sources including filings of public companies, relationships with certain private companies, and monitoring of website traffic.

To estimate the size of the U.S. gambling market under the Frank bill, PwC adjusted H2GC's forecast to take account of potential state opt outs and the prohibition on sports betting. Two scenarios were considered regarding state opt outs. Under the *low* opt-out scenario, states were assumed *not* to opt out with respect to online games that currently are authorized in land-based form within their jurisdictions. Under the *high* opt-out scenario, it was further assumed that 10 states that prohibit online gambling would

¹ The federal wagering excise tax does not apply to certain land-based forms of wagering because the definition of taxable wagering excludes, among other things, games where winners are determined and prizes distributed in the presence of all the bettors. We assume internet gambling would not qualify for this exemption and would therefore be subject to the tax.

fully opt out regardless of the fact some forms of land-based gambling are authorized in these states (i.e., Illinois, Indiana, Louisiana, Michigan, Nevada, New Jersey, New York, Oregon, South Dakota, and Washington).

Under the legislation, licensed online gambling operators would be required to pay the existing federal wagering and corporate income taxes as well as a new licensing fee applicable to deposits into online gambling accounts. In addition, licensees would be subject to a separate and more comprehensive obligation to provide information returns regarding winnings to the Internal Revenue Service and players. As under present law, players would be subject to individual income tax on net winnings.

Over the FY 2010-19 period, the federal revenue effect of the proposal (including revenues from the wagering tax, licensing fee, and individual and corporate income taxes) is estimated to range from \$13.0 billion under the *high* state opt-out scenario to \$25.9 billion under the *low* state opt-out scenario (see Table E-1 below). In each case, about 60 percent of the revenue is attributable to individual income taxes, 20 percent is due to the wagering tax, 15 percent is due to the licensing fee, and 5 percent is due to the corporate income tax.

Table E-1. Revenue Effect of the Proposal, FY 2010-19
(Fiscal years, millions of dollars)

Revenue source	2010	2011	2012	2013	2014	2010-14	2010-19
Low State Opt-Out Scenario							
<u>Total</u>	<u>\$858</u>	<u>\$1,515</u>	<u>\$1,917</u>	<u>\$2,277</u>	<u>\$2,619</u>	<u>\$9,186</u>	<u>\$25,852</u>
License Fee	127	221	282	335	386	1,351	3,836
Wagering Tax	191	328	416	499	578	2,012	5,706
Individual Income Tax	449	840	1,089	1,305	1,510	5,193	14,851
Corporate Income Tax	92	126	130	137	145	630	1,458
High State Opt-Out Scenario							
<u>Total</u>	<u>\$434</u>	<u>\$763</u>	<u>\$965</u>	<u>\$1,149</u>	<u>\$1,325</u>	<u>\$4,637</u>	<u>\$13,049</u>
License Fee	61	105	134	160	185	645	1,831
Wagering Tax	98	167	212	255	296	1,029	2,916
Individual Income Tax	230	429	555	667	774	2,655	7,590
Corporate Income Tax	45	62	63	67	71	308	711

Source: PricewaterhouseCoopers calculations. Effective date assumed to be January 1, 2010.

Under H.R. 2267, Internet betting on all amateur and professional sports events in the United States would remain prohibited under the Professional and Amateur Sports Protection Act. Past versions of the legislation would have allowed Internet betting on sporting events unless the sports leagues opted out of the regulatory regime. For purposes of this report, UC Group asked that we include an estimate of the impact of the legislation as if it allowed sports betting and the leagues did not opt out. Under these assumptions, we estimate the legislation (as modified) could increase federal revenues by as much as \$62.7 billion over the 2010-19 period (see Table E-2).

**Table E-2. Total Increase in Revenues under Alternative Assumptions,
With and Without Sports Betting
(Fiscal years, millions of dollars)**

Scenario	2010	2010-14	2010-19
<u>H.R. 2267 as Introduced (Sports Betting Excluded) and:</u>			
High State Opt-Out Rate	\$434	\$4,637	\$13,049
Low State Opt-Out Rate	\$858	\$9,186	\$25,852
No States Opt Out	\$1,605	\$17,266	\$48,592
<u>H.R. 2267 Amended to Include Sports Betting, and:</u>			
High State Opt-Out Rate	\$504	\$5,459	\$15,487
Low State Opt-Out Rate	\$1,031	\$11,238	\$31,941
No States Opt Out	\$2,007	\$22,025	\$62,715

Source: PricewaterhouseCoopers calculations. Effective date assumed to be January 1, 2010.

PwC previously prepared a revenue estimate of the legislation in September 2008. This report contains revised estimates based on updated projections from H2GC of the U.S. online gambling market under current law and the Frank bill. The revenue estimates in this report are approximately 21 percent larger than those in the September 2008 report. The increase in the estimate primarily is attributable to the revised projections from H2GC, which were partially offset by other revisions.