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**Presenter: Dave Malone  
and Susan Arland**

**The Tangled Web: Internet  
Gambling**

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**The Tangled Web:  
Internet Gambling**

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**Introduction**

- A. Internet Gambling: what, where, why, and how?
- B. Legislation/Litigation Summary and Update.
  - Federal
  - State
  - World Trade Organization – Antigua
- C. Pending Legislation & Future Issues.

**I-Gaming: What is it?**

- A. Gambling Defined
  1. Risking something of value (**consideration**);
  2. On an outcome beyond bettor's control (**chance**);
  3. For something of value (**prize**).
- B. Internet – Complex web of computer networks in communication with one another. May involve multiple jurisdictions.

**Elements of Gambling**

- Consideration
  - Direct vs. Indirect
    - Direct - Majority opinion only direct wager constitutes consideration. Does not include incidental costs.
    - Indirect – fees for internet access, text message fees, redemption of points.
    - Flexible entry fees – free entry with additional entries for larger purchase, more time, etc.

**Elements of I-Gaming**

- Chance
  - Majority Rule: Does skill or chance predominate the activity? (Predominance Test).
  - Chance spectrum:
    - Slots (pure chance) - chess (pure skill)
    - Mixed results for games such as poker, where both elements are present.
    - Minority rule – does the activity appeal to “gambling instinct”?

## I-Gaming: History and Scope

- Prize
  - Anything of value –
    - Money
    - Credit
    - Merchandize
    - Redemption points

## History and Scope Continued

- January 17, 1995 – First Internet bet.
- Currently – Licensed in over ninety countries.
  - 2005 estimate - 23 million Internet gamblers.
  - Approximately 2,500 websites offering gambling with an estimated \$10 billion in revenues.
- Gray area games:
  - Video games (\$7.5 billion/year);
    - On-line tournaments and/or direct play.
  - Web-gaming – MSN, Yahoo, etc. Free games with pay-for-play option.
  - Redemption sites, fantasy leagues, “texting” contests.

## History and Scope Continued

- Major Internet Gambling Countries.
  - Central America: Belize, Costa Rica, Panama.
  - Caribbean: Antigua-Barbuda, Dom. Republic, Grenada, Curacao, U.S. Virgin Islands\*.
  - Europe: Alderney, Isle of Man, Malta, U.K.
  - North America: Canada - Kahnawake Res. (Quebec); United States (horseracing).

## Demographics of Internet Gamblers

- |                        |                         |
|------------------------|-------------------------|
| ■ <u>United States</u> | ■ <u>United Kingdom</u> |
| ■ 52.34% male          | ■ 50.71% male           |
| ■ 47.66% female        | ■ 49.29% female         |
| ■ Age                  | ■ Age                   |
| ■ 18-24 – 6.88%        | ■ 18-24 – 15.30%        |
| ■ 25-34 – 14.91%       | ■ 25-34 – 21.91%        |
| ■ 35-44 – 19.64%       | ■ 35-44 – 23.78%        |
| ■ 45-54 – 23.95%       | ■ 45-54 – 15.58%        |
| ■ 55+ – 34.62%         | ■ 55+ – 23.43%          |

## Federal Legislation & Litigation

- Interstate Wire Act (18 U.S.C. § 1084 et seq.)
  - Four major elements:
    1. being engaged in the business of betting or wagering;
    2. knowingly using a wire communication facility;
    3. for the transmission in interstate or foreign commerce of bets or wagers or information assisting in their placement;
    4. on any sporting event or contest.
  - Penalty – fines and/or imprisonment of not more than two years.

## Federal Legislation Cont'd

- Recurrent Wire Act Issues.
  - Application to Internet? Adopted in 1961 to fight organized crime (bookmaking).
  - Exemption for “placing of bets or wagers on a sporting event or contest from a State or foreign country where betting on that sporting event or contest is legal into a State or foreign country in which such betting is legal.” 18 U.S.C. 1084(b).
  - Arguably limited to “sporting” events or contests.

## Federal Legislation

- Unlawful Internet Gambling Enforcement Act (UIGEA), 31 U.S.C. §§5361-5367.
- Adopted in October of 2006 as a rider to the "SAFE" Ports Act.
  - Vote against the UIGEA was vote against improving Homeland Security measures for U.S. ports.
  - Clarifies the act of gambling occurs both where the operator is located and where the gambler is located.
  - Does not apply to the Interstate Horseracing Act.
  - Does not render any Internet gambling illegal that was not already illegal.

## UIGEA Cont'd

- Enforcement Provisions.
  - §5363 – Prohibits gambling operators from accepting money transfers for unlawful internet gambling from U.S. customers.
  - §5364 – "Designated payment system" providers must identify and block such monetary transfers.
  - §5365 – Remedies: (A) Injunctive relief may be sought by U.S. or State Attorney General; (B) Fines and/or prison terms not to exceed five years.

## UIGEA Cont'd

- Definitions:
  - Wager – staking something of value on the outcome of a contest of others, sporting event or game of chance, including lottery tickets.
  - Excluded activities:
    - Securities/commodities exchanges; derivatives; and insurance contracts.
    - Fantasy sports/simulation leagues.

## UIGEA Cont'd

- Definitions.
  - "Designated payment system" means "any system utilized by a financial transaction provider that . . . [federal agencies] jointly determine by regulation or order, could be used in connection with, or to facilitate, any restricted transaction."
  - "Financial transaction provider" means any creditor, financial institution, electronic fund transfer terminal operator "or other participant in a designated payment system."

## UIGEA Exemptions

- Interstate Horseracing.
- Intrastate transactions - those initiated within a single state, if authorized and regulated by state law.
- Intratribal transactions – those wagering transactions initiated within a single reservation or between two or more reservations where authorized.

## UIGEA cont'd

- Regulations pending.
  - Issued on October 7, 2007, the proposed regulations generated significant criticism.
  - Rules do not specify which gambling activities are illegal because UIGEA defers to underlying State and Federal law.
  - Apply only to U.S. payment processors.
  - HR 5767 – prohibit adoption.

## UIGEA Regulations cont'd

- Federal hearing conducted on April 2, 2008.
  - Sununu-Domenici letter expressing concern for burden placed on U.S. financial institutions.
  - Criticism from banking industry officials.
  - Consensus concern that neither the Act nor the proposed rules define "unlawful Internet gambling" and therefore the financial industry will reject legitimate transactions.

## Interstate Horseracing Act

- 15 U.S.C. § 3001 et. Seq.
- Amended in 2000 by expanding definition of "interstate off track wager" to include pari-mutuel wagers transmitted between states via telephone or electronic media.
- Washington – RCW 67.16.260/Chapter 260-49 WAC authorized advanced deposit wagering in 2004. Four licensed Internet gambling sites.

## Federal Litigation - Criminal

- U.S. v. Ross, (98-CR-01174, U.S.D.C. So. Dist. New York).
  - Island Casino, a Curacao-based sportsbook, at which FBI placed bets in 1997 and 1998.
  - Defendant Ross was indicted under Wire Act and RICO.
    - Argued bets did not become wagers, until accepted by Island Casino. Therefore, activity occurred in Curacao.
  - Court held 1084(b) exemption applies only to transmission of information assisting wagers, not the wagers themselves.
    - Because Island had ability to accept bets, bettors were bound as soon as wagers placed.

## Federal Litigation Cont'd

- U.S. v. Cohen, 260 F.3d 68 (2<sup>nd</sup> Cir. 2001).
  - Cohen owned World Sports Exchange, based in Antigua, and was convicted of eight counts of Wire Act violations.
  - Cohen argued 1084(b) exemption applied.
  - Court disagreed: Two conditions must be met: (1) betting must be legal – not just a non-criminal act - in both locations; and (2) transmission of betting information does not include wagers.
  - Betting was not legal in New York. No need to address issue of account wagering.
  - U.S. Supreme Court denied *writ of certiorari*.

## Federal Litigation Cont'd

- Sterling Suffolk Racecourse v. Burrillville Racing Ass'n, 989 F.2d 1266 (1<sup>st</sup> Cir. 1993).
  - Civil case involving competing racetracks in Boston and Rhode Island; Burrillville running OTB wagering without consent of all tracks (Sterling).
  - Unlike Ross and Cohen, appellate court rule that the Wire Act exemption did apply because activity was legal in both sending and receiving jurisdictions.
  - No distinction between actual bets/wagers and information assisting in placement of such.

## Federal Litigation Cont'd

- U.S. v. Bala, 489 F.3d 334 (8<sup>th</sup> Cir. 2007).
  - OTB phone wagering in North Dakota on out of state races.
  - Violation of Wire Act if defendant transmitted information assisting in placement of wagers, *unless* wagering in event was legal in both jurisdictions.
    - OTB wagering was legal in North Dakota and where the races occurred.
  - Defendant was acquitted and appellate court upheld decision. Court noted the nature of the activity (wager or information assisting) had not been raised and was not addressed.

## Federal Litigation Cont'd

- U.S. v. D'Ambrosia, 313 F.3d 987 (7<sup>th</sup> Cir. 2002).
- Defendants operated Gold Medal Sports Book from Curacao. Complex tax shelter scheme employed by disbarred attorney. Over \$400 million not reported.
- Defendants plead guilty to Wire Act violations and tax fraud. At sentencing, court concluded a four-level increase in offense level because defendants were leaders of criminal activity. Defendants appealed grouping of Wire Act violations with tax issues.
- Court determined the tax conspiracy violations incorporated the Wire Act violations.

## Federal Litigation Cont'd

- U.S. v. BetonSports, (06-CR-00337 E. Dist. Missouri).
- Sports betting site based in Costa Rica. Owner arrested in 2006 while changing planes in Dallas.
- 22-count indictment issued in June of 2006.
  - Wire Act, RICO, etc.
- Case ongoing – motions filed April 11, 2008.

## Federal Litigation Cont'd

- U.S. v. NETeller, (07-CR-00597, U.S.D.C. S.D. New York).
- Internet payment service. Processed over \$7.3 billion in 2005. According to company, 95% of its revenues came from internet gaming companies.
- Based on the Isle of Man, publicly traded in United Kingdom.
- Proprietors, Canadian citizens, were arrested in 2007. Both plead guilty to violations of Wire Act and UIGEA.
  - Prison sentences, fines, and personal forfeiture of \$100 million.
- Company agreed to deferred prosecution and forfeiture of \$136 million in profits from U.S. wagers.

## Federal Litigation - Civil

- Jubelirer v. MasterCard, 68 F.Supp. 2d 1049 (1999).
- Plaintiff lost approximately \$25 on internet site and sued MasterCard for RICO violation.
- Court granted MasterCard's motion to dismiss concluding there were insufficient facts to show RICO operation.
- Facilitating an internet operation via funds transfers was not enough to establish RICO enterprise.

## Federal Litigation - Civil

- In re MasterCard, 313 F.3d 257 (5<sup>th</sup> Cir. 2002).
- Underlying cases (33) involved a class action suit against MasterCard alleging the company aided and abetted internet casinos in violation of U.S. law. (Wire Act/RICO).
- MasterCard's motion to dismiss was granted by district court, concluding Wire Act does not apply to internet games of chance – only sports wagering.
- Court of Appeals upheld the decision and affirmed lower court ruling re: scope of Wire Act, i.e. it does not apply to casino-style gambling.
- U.S. Department of Justice maintains Wire Act prohibits all forms of internet gambling.

## Washington State Legislation

- RCW 9.46.240 –
  - Whoever knowingly transmits or receives gambling information by telephone, telegraph, radio, semaphore, the internet, a telecommunications transmission system, or similar means, or knowingly installs or maintains equipment for the transmission or receipt of gambling information shall be guilty of a class C felony.
  - Underlined sections adopted in 2006 as part of Sub. Senate Bill 6613, which also prohibited the lottery from selling tickets on the internet.

## Washington Litigation

- Betcha.com v. Washington State Gambling Commission, (Thurston Co. No. 07-2-01334-0).
  - Peer to peer site. Proprietor argued gambling not present because participants did not “risk” anything. Bettors could refuse to pay losing wagers. Participants would be rated similar to eBay.
  - Summary Judgment in favor of WSGC. Case on appeal.
- Rouso v. Washington, (King Co. No. 07-2-22438-6).
  - Lee Rouso, attorney & poker player, is suing the State alleging the 2006 amendment to RCW 9.46.240 violates the constitution (cruel & unusual punishment; commerce clause).
  - Trial set for May 15, 2008.

## WTO Dispute

- March 2003 – Antigua and Barbuda start dispute resolution process of World Trade Organization (WTO) to challenge U.S. prohibition on cross-border gambling.
  - Negotiations followed by referral to three-member Dispute Panel.
- March 2004 – WTO Dispute Panel issues confidential report in favor of Antigua.

## WTO Dispute

- Negotiations resume, U.S. refused to modify its position. November 2004, Panel Report released to public.
- January 2005, U.S. appealed Panel Report.
- April 2005, WTO Appellate Body upheld Dispute Panel Report.
  - Four key findings noted.

## WTO Dispute

1. U.S. made commitment to free trade in gambling services via GATS.
2. U.S. adopted measures that interfered with its obligation to provide gambling services with Antigua.
3. U.S. prohibitions limited service providers in Antigua, in violation of GATS.
4. U.S. could not invoke “moral defense” clause re: GATS violation.

## WTO Dispute

- Dispute Panel Report provided for U.S. could comply by:
  1. Allowing access to U.S. markets; or
  2. Prohibiting all forms of internet gambling in the U.S.
- April 2006 – Compliance period expired. U.S. maintained existing criminal statutes addressed all forms of internet gambling, including horseracing.
  - In re MasterCard and Interstate Horseracing Act?

## WTO Dispute

- June 2006 – WTO Compliance Panel concluded U.S. failed to comply.
- July 2006 – Antigua requested another WTO panel address the issue.
  - U.S. argued it had come into compliance.
- March 2007 – Compliance Panel issued its report. Three significant findings noted.

## WTO Dispute Cont'd

1. U.S. took no action to comply with Panel Report and it remained out of compliance;
2. U.S. was not entitled to reargue the case;
3. Even if the U.S. were allowed to reargue the case, based on the evidence, the "morals defense" would still fail.

## WTO Dispute Cont'd

- Antigua entitled to impose trade sanctions against U.S.
- 2007 – U.S. declared withdrawal from commitment re: cross-border gaming.
  - Withdrawal required compensation of "any affected" WTO members.
  - Claims then filed by: European Union, Costa Rica, Canada, Macau, India, Australia, Japan.

## WTO Dispute Cont'd

- U.S. settled with Australia, E.U., Canada, India, and Japan.
  - Granted compensation access to U.S markets for postal/courier service, R&D, technology testing, and warehousing.
- Antigua filed a claim for up to \$3.4 billion.
- December '07 – Antigua awarded \$21 million annual compensation.
- January 2007 – Antigua and Costa Rica file additional claims. Other countries unresolved.

## Pending Federal Legislation

- HR 2046 – Barney Frank (D-MA). Internet Gambling Regulation and Enforcement Act (IGREA). Legalize Internet gambling and create federal regulatory framework.
- HR 2140 – Shelley Berkley (D- NV). Academy of Sciences to study Internet gaming and report to Congress.

## Pending Federal Legislation

- HR 2607/HR 5523 – Jim McDermott (D-WA). Build on Frank bill by amending revenue code. Internet gaming tax.
- HR 2610 – Robert Wexler (D-FL). Exempt skill games (poker) from Internet prohibition.
- HR 5767 – Barney Frank & Ron Paul. Prohibit adoption of UIGEA regulations.

## Future Issues

- Canada – Federal efforts to shut down Kahnawake Internet gaming operations.
- WTO Part II - U.S. criticism of United Kingdom as a major conduit for money laundering via Internet gambling.
- New gambling media – mobile phones, Second Life, etc.