“The Unlawful Internet Gambling Enforcement Act - Is there a better alternative?”

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September 30th, 2006 saw a tipping point in the world of internet gaming. The addition of the ‘Unlawful Internet Gambling Enforcement Act’ to the Safe Ports Act as it passed through Congress, was seen as effectively closing the door on internet gambling in the US and with it half its global market. U.S. President George W. Bush signed the law on Oct. 13th. By July 10th, 2007 the necessary tools to bring the Act into full force will be in place.

The perceived loss of the largest market for online gaming saw massive falls in the share prices of some of them, shortly followed by the collapse of at least one firm, redundancies and consolidation. Sportingbet plc sold its US interests for $1. Banks, hitherto courting the firms have threatened withdrawal of services.

Yet the Act did not, in itself make internet gaming illegal, The laws on this activity already existed and many had been in force for years.

So why did this Act have such an impact? This article looks at the issues surrounding internet gaming and the attempts to control it. It also compares the US approach with that taken by jurisdictions such as the UK and Gibraltar and argues that, the regulation using tools similar to those already in place in the financial sector will deliver the environment the legislatures’ seek, the prohibition approach will simply accentuate the problem.

The US approach

In the US most gaming statutes are state based. The main pieces of national legislation which are seen to impinge upon this activity are the Federal Wire Act 1961 (Act 18 U.S.C 1084) which makes it illegal to use the telephone or telecommunications to conduct illegal gambling business (though arguably this is limited to bets on sporting events or contests) and the Travel Act (Act 18 U.S.C 1952) which covers the use of interstate or foreign commerce to distribute the proceeds of any business or enterprise involving unlawful activities. Both of these are also predicate offences for the draconian Racketeer Influenced and Corrupt Organizations (RICO) provisions which exposes offenders to up to twenty years in jail. Money laundering and tax evasion statues may also come into play.

Federal and State statutes had already been used against internet gaming companies. Indeed, in 2006 US authorities arrested visiting executives from two online gaming companies, David Carruthers from BETonSPORTS Plc and Peter Dicks from Sportingbet Plc.

The main feature of the 2006 Act is to prohibit anyone engaged in the business of betting and wagering from accepting any financial instrument for unlawful internet gambling (restricted transactions). Furthermore it provides for the
publication of policies and procedures requiring those operating payment systems to identify and prevent restricted transactions. Offences are punishable by up to five years imprisonment.

Yet the US has always been inconsistent in its approach to gambling. Whilst number of states have passed explicit legislation banning internet gaming (Illinois, Louisiana and Nevada for instance), there are the Interstate Horseracing Act and Indian Gaming Regulatory Act, which enable gambling and both of which have internet gaming dimensions.

Most states employ a lottery as a means of public finance and to allow several other forms of gambling as well. In fact, according to a 2004 report to Congress, at least forty-six states permit charitable bingo; forty-three allow pari-mutuel (or tote) betting; thirty-seven have lotteries; twenty-nine have Indian gambling establishments; and thirteen allow casino or riverboat gambling. The report stated that Americans spend almost $73 billion a year on legalized gambling.

The 2006 Act did not create any new class of unlawful internet gambling. Indeed, the definition of bet or wager under the 2006 Act, expressly excludes some activities such as games or contests where participants do not risk anything of value, other than personal effects or points or credits (than can only be redeemed for further participation in games or contests). This means that free play on poker sites will be legal. Under certain criteria fantasy or simulation sports games will also be permitted.

So why did the 2006 Act have such an impact? The reason is that it attacked the most critical element of internet gaming, money transmission. Without a mechanism to get money from and make payments to participants, internet gaming cannot operate. Therefore by making the acceptance of financial instruments by unlawful gaming operations an offence, the providers of such instruments may be aiding and abetting.

In general the banks and other providers, who do not want to risk exposure to prosecution in such a vital market to their overall businesses, are not bothered by technical legal arguments on what is and what is not covered by the definition of “unlawful internet gaming”. They therefore began to retrench from providing this service. This included, for example, withdrawing facilities from those operators who did not commit to completely pulling out of the US market. Given that the US represented half the global market, and for some operators, virtually all their business, the resultant collapse was inevitable.

The alternative approach

This approach has been one of marked contrast to that of the US. Like some other EU jurisdictions (for example Belgium) the UK plans, when the final elements of the 2005 Gambling Act come into force in September 2007, to allow online gaming to operate within a formal regulatory environment. Gibraltar already has such a regulatory environment.
At a conference held at the end of October 2006 in Ascot, and attended by representatives of 32 jurisdictions (but not the United States who declined the invitation), Tessa Jowell, the British Culture Secretary, said that Britain wanted to welcome online operators. "We will welcome them here because we believe that by allowing those who want to gamble to do so over the counter, not under the counter, is the best way to protect children and vulnerable people and keep out crime."

UK has a particular interest in this area. Research has found that internet there are almost a million regular internet gamblers in the UK, making up about a third of the European total. The average sum staked by web gamblers was £1,000 a year.

The key issue is whether Britain becomes attractive will be the revisions to its tax regime. However one further concern to a number of gaming companies will inevitably be the impact of the UK’s 2003 Extradition Act, recently thrust into the attention of many businessmen by the case of the “NatWest Three”.

Indeed at the Ascot meeting, UK Sports Minister Richard Caborn told a news conference that Britain would not protect UK online gaming executives from extradition requests if they took Internet bets from countries in which they were illegal. This was, in some ways a curious statement, the Extradition Act itself requires something to be an extradition offence before someone can be extradited to the US.

Under section 64 of the Act, an extradition offence is either something done in the US which would be an offence not just in the US but also an offence under UK law or an offence that occurs outside the US which would be punishable in the US and in corresponding circumstances the equivalent conduct would constitute an extra-territorial offence against the law of the UK. A minimum punishment of not less than 12 months in jail for the offence is also required.

As internet gaming will be licensable in the UK, the only way that extradition could occur is if other offences such as money laundering or tax evasion were included in the request. However, this does leave an uncertainty as the US Department of Justice might seek to include additional offences in order to activate extradition proceedings.

**Prohibit or regulate?**

So why do mature jurisdictions come up with such diametrically different solutions to the same issue?

The US public arguments of those against internet gambling can be summed up as follows:

- Internet gaming is linked to organized crime
- It is rife with fraud
- It is ideal for money laundering
- It threatens the integrity of amateur and professional sports
• It is available to the vulnerable, particularly children (who can run up debt on their parents’ credit cards)

But are these arguments true, and, if so, is prohibition the answer?

On the first, there are, no doubt, gaming companies with links to organized crime, but there are far more that have none. Party Gaming and 888 are listed on the London Stock Exchange (Party Gaming until recently was a FTSE 100 company), B-Win is listed on the Vienna Exchange. We do not ban other business sectors because some people within them may be criminals. Instead we conduct checks on the managers and controllers of those businesses to ensure we keep the criminal elements out. This has worked in banking, insurance and securities for years all of whom otherwise would be vulnerable to criminal infiltration.

Similarly there will be fraudulent sites, just as the internet has spawned new types of banking and security fraud. Some sites will cheat, some may misuse credit card details. Yet in general we do not seek to ban the legitimate as a solution, rather we look for ways to reduce or eliminate the fraudsters. Indeed the customers of gaming sites have developed one of the most advanced consumer driven protection mechanisms in existence. They have done this through the simple approach of talking to each other. There are a plethora of gaming chat rooms. Go onto these and you will see that the gamblers very quickly warn each other about slowness in paying, poor quality service and scams. Indeed these put others on alert far faster than a traditional regulator can. In any event, regulated sites will be far less likely to be fraudulent.

The argument that internet gambling is ideal for money laundering ignores some basic factors. Firstly it cannot be used for placement. The money already has to be within the financial system. Whilst it is possible to use it as part of the layering process it is not ideal and there are far better methods (including buying shares). Additionally in regulated jurisdictions gaming sites are covered by that jurisdictions anti money laundering provisions and are subject to regulation and monitoring. No doubt money has been laundered through gaming sites but it is no more risky than other finance based businesses and far less risky than most. In fact the greatest threat of its use in this way would be to drive the industry underground and into the hands of criminals.

The gaming industry where it is linked to sports has always had the ability to undermine a sport’s integrity. Players and officials can be bribed or blackmailed. Internet gaming did not create this; its demise would not eliminate it. Indeed by driving it underground and therefore immune from scrutiny the position can get worse. A better, proven route is for sport and gaming to cooperate to discover and defeat the cheats. It is in both their interests to do so. Such cooperation already exists in other areas of gambling. Again a parallel with others sectors exists. There are laws to prevent market abuse so helping to prevent insider trading and market manipulation. Similar investigative and enforcement powers can be used in the sporting arena.
The impact on children is, by its nature, emotive. The internet generally provides a Pandoras box and to reduce juvenile exposure to the less savoury elements is clearly an important goal. Yet, at least internet gaming (apart from practice areas) is not free. You need money and a payment mechanism to play. This will exclude most children from participation. To claim internet gaming specifically encourages children stealing from their parents is a somewhat bizarre accusation. Those tempted to steal their parents credit cards are just as likely to do so to buy drugs, tobacco, alcohol or even DVD’s and games from internet sites. If they do so, it is highly likely that their parents will discover the theft when their next credit card bill arrives. The debt itself may be unenforceable. Furthermore by continuing to allow fantasy sport games, the 2006 Act does not even prevent the risks its proponents claim children are exposed to

So what should be the response?

No one wants to see addicted gamblers and their families reduced to penury. However, is this a good enough reason to ban a leisure activity that is harmless and pleasurable to the vast majority of its participants. Alcohol can wreck lives, but we seek to control its excesses not ban it. Freedom is meaningless unless people are permitted to act in a way that others morally disapprove of (within limits of course).

The key is effective regulation not prohibition. By licensing and regulating gaming sites, jurisdictions can control the internet gambling environment. Illegal sites will exist but players will generally choose the legitimate and safe. Ban the legitimate and players (there will always be players) will be forced into the very areas the legislature is trying to save them from.

So what should a regulatory environment contain. Clearly there must be vetting of those seeking licenses. They must also have the financial resources to ensure they can meet any debts owing. Games must be fair and seen to be such. There must also be stringent safeguards to prevent underage gamblers and to help addicted gamblers (for example by limiting time on site, amount spent or having voluntary exclusion periods). Funding to support charities to help addicts should also be a priority.

In this way the legitimate can provide a service and leave no vacuum for the illegitimate to enter into.

Where to from here?

According to the media, the U.S. accounted for half of the $12 billion Internet gambling market last year. Internationally internet gaming has grown from nothing in the early 1990’s to a major leisure activity with over 1800 gaming sites. It provides greater choice and, through competition, better value. For governments it is a source of revenue. As a result of its popularity on the internet, poker is now a even a televised activity.
To drive internet gaming underground either on grounds of protectionism or for “moral” reasons is foolish. It will only achieve the results that the advocates of banning are ostensibly seeking to avoid.

The alternative approach, which is the likely EU model, provides a sensible, proactive model for licensing and regulation. A number of offshore centres such as Gibraltar have already pursued this line. Once such a model is established consumers will generally follow the safe, legitimate path.

Furthermore the establishment of international standards, like those for banking and fighting money laundering will allow the international community to coordinate and cooperate against the unregulated and fraudulent elements. Jurisdictions which pride themselves on providing an unregulated environment will find their gaming industry marginalised and minimised. But we must create a legitimate supply for a genuine demand. It is only in this way that a safe environment for players can truly be created.