
INTERNET GAMING: IS IT TOO LATE TO REBOOT?

By Mark Brnovich & Tom Gede*

As the 111th Congress wound down in December 2010, Senate Majority leader Harry Reid was busy circulating legislation that would authorize Internet poker in the United States.¹ Earlier in the year, similar legislation to allow Internet gaming was being advanced by Representative Barney Frank. H.R. 2267 ultimately passed the House Financial Services Committee by a nearly two to one margin² with demonstrable bipartisan support.³ While these most recent efforts to legalize Internet gaming were not successful at reaching a full floor vote in the House, it is a good bet that efforts to expand gambling on the Internet will continue at both the federal and state level.

The definition of what constitutes “gambling” has changed little throughout history. Essentially, it is the act of risking something of value in order to have an opportunity to win something based upon chance,⁴ often simplified as having three elements—prize, consideration, and chance. Early forms included casting lots or throwing dice.⁵ Throughout history, civilizations have struggled to determine whether gamblers should be prosecuted, ostracized, or left to their own devices.

In early colonial America, lotteries were popular and were used to finance major building projects. Ben Franklin ran the Philadelphia lottery, and the Continental Congress authorized a lottery to fund the Continental Army during the Revolutionary War.⁶ Along with gambling, however, came social costs. These included crime and corruption.⁷ The public’s attitude toward gambling and lotteries was especially impacted by unscrupulous organizers and promoters who rigged games or failed to award promised prizes. For example, the United States Supreme Court held that the government was responsible for paying a lottery winner after the promoter failed to do so.⁸ Sympathy for defrauded victims and concern over corrupt operators, however, did not signify an antipathy for gambling per se.

Congress stepped in to prohibit the interstate transportation of lottery tickets. While it may seem uncontroversial today, a divided Court decided that Congress had the authority pursuant to the Commerce Clause and its police powers to prohibit the interstate transportation of lottery tickets.⁹

Prior to passage of the Unlawful Internet Gambling Enforcement Act of 2006 (“UIGEA”), the federal government relied upon the 1961 “Wire Act” to prevent betting or wagering via the Internet.¹⁰ But questions were raised about whether the Wire Act applied only to betting on sporting contests, not casino-style games.¹¹ To help further combat the infiltration of organized crime into gambling, Congress enacted the Illegal Gambling Business Act.¹² The legislation was part of the

Organized Crime Control Act of 1970 and makes operating an illegal gambling business with five or more people a crime.¹³ However, federal prosecutors are limited in their use of this statute because, unlike brick and mortar operations, one or two people can easily operate an Internet gambling website anywhere in the world.

Other federal efforts to control the spread of gambling, including the passage of the Professional and Amateur Sports Protection Act (“PASPA”) in 1992.¹⁴ PASPA makes it illegal for a state to allow sports betting (other than on horse or dog racing) unless the state had authorized legal sports betting as of 1991.¹⁵ With the proliferation of gambling in the past decade, challenges to PASPA have become inevitable. For example, the Third Circuit Court of Appeals recently upheld the Act, holding that it wasn’t an unconstitutional infringement on state sovereignty.¹⁶ However, with hundreds of millions of dollars of annual revenue at stake, it is likely that states will continue to challenge PASPA or push for its repeal.¹⁷

While the federal government has attempted to limit illegal gambling, the Internet has made gambling easier and more accessible. One gambling consulting firm estimates online gambling accounts for about \$29 billion in revenue annually, about \$12.5 billion coming from Europe.¹⁸ Some authorities predict, however, that by the year 2015, the Internet gambling industry will bring in \$528 billion annually worldwide.¹⁹ Further complicating the matter is the trend toward removing legal restrictions on Internet gambling. For example, the United Kingdom passed The Gambling Act in 2005 that allows the regulation and licensing of the online gambling industry.²⁰ Although the U.K. probably has the most well-developed system of gambling laws and regulations, other countries are starting to allow more online gambling. Earlier this year, France allowed private companies to take bets online in competition with state-run sites.²¹ Denmark approved similar legislation, and Italy now allows for high-stakes poker and other casino games and collected about €150 million from taxes on online gambling last year.²² With Internet gambling coming to Canada, it is only a matter of time before proponents of Internet gambling argue that unless the United States allows Internet gambling, it will fall behind the rest of the world.²³

However, in an effort to address and expressly prohibit Internet gambling in the United States, Congress passed UIGEA in 2006. The UIGEA prohibits financial institutions from knowingly accepting transactions related to online gaming.²⁴ The UIGEA defines unlawful Internet gambling as knowingly transmitting a bet or wager that in some way utilizes the Internet and is unlawful under applicable state, federal or tribal law where the bet or wager is “initiated, received, or otherwise made.”²⁵ Bets or wagers can also include “the purchase of a chance or opportunity to win a lottery or other prize (which opportunity to win is predominantly subject to chance)” or “any instruction or information pertaining to the establishment or movement of funds by the bettor or customer in, to, or from an account with the business of betting or wagering.”²⁶ It does not include intrastate or intra-tribal bets or wagers that are legal under the

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Interstate Horseracing Act, the Professional and Amateur Sports Protection Act, the Gambling Devices Transportation Act, or the Indian Gaming Regulatory Act.²⁷

Although “unlawful Internet gambling” lacks a comprehensive definition, the Third Circuit declared that it is not unconstitutionally vague.²⁸ In *Interactive Media Entm’t & Gaming Ass’n v. Attorney Gen. of the U.S.*, a group representing Internet gaming providers sued to enjoin enforcement of the UIGEA by alleging that it was unconstitutionally vague and interfered with individuals’ privacy rights to gamble in their own homes. The court rejected the vagueness claim because the UIGEA clearly states that Internet gaming is determined by applicable federal law, or the law in the state where the bet is placed or received.²⁹ The court reasoned that the UIGEA provides a “person of ordinary intelligence with adequate notice of the conduct that it prohibits.” That Internet gambling may be illegal in some states and legal in others does not render the UIGEA unconstitutionally vague.³⁰ Regarding the group’s privacy claim, the court did not find the group’s reliance on the Supreme Court’s rationale in *Lawrence v. Texas* convincing and said that an individual’s privacy interest in gambling at home is not a fundamental personal right.³¹ The court stated, “[G]ambling, even in the home, simply does not involve any individual interest of the same constitutional magnitude” as the private human conduct and sexual behavior at stake in *Lawrence*.³² Thus, although gambling laws vary from state to state, the UIGEA’s definition of “unlawful Internet gambling” is likely to stand up to court challenges in the future.³³

Aside from the general criticism that the UIGEA does not define unlawful Internet gambling, some say that the UIGEA does not do enough to effectively curb online gambling, while others say the burden imposed on financial institutions is too heavy. Critics say that the UIGEA leaves open too many loopholes that allow for online gamblers to send money to online gaming operators.³⁴ For example, it may be difficult to block overseas payment processors.³⁵ Also, one critic alleges that the UIGEA puts an undue burden on financial institutions because it saddles them with the cost of detecting and blocking restricted transactions, amounting to “an unjust appropriation of private resources for law enforcement purposes.”³⁶ Others have argued, however, that the UIGEA’s requirement that financial institutions must have actual knowledge of a restricted transaction and not a lesser negligence standard coupled with no penalty for failure to comply with the rules, reflect a minimal burden on the financial system.³⁷

While Congress is attempting to limit Internet gambling, several states are making efforts to introduce some form of legalized on-line gambling. Both California and New Jersey legislators have recently pushed for “intranet” gambling. Legislators in Florida have also introduced legislation that would regulate and tax online poker. Additionally, several states are considering launching on-line intrastate lotteries. Presumably, such activities would have to be wholly intrastate. To comply with UIGEA, Internet gambling would have to be lawful in both the state (or tribal land) in which a bet is originated and the state (or tribal land) in which the bet is received or processed by the gambling business.³⁸

With government budgets tight and public attitudes toward gambling shifting, it is little surprise that efforts are now underway to roll back UIGEA and allow Internet gambling. Representative Frank’s Bill, H.R. 2267, would overturn portions of UIGEA. While the bill was voted out of committee,³⁹ it failed to reach the House floor before the Congress adjourned. Observers speculated it would be folded into “must pass” legislation, much as UIGEA was attached to the SAFE Port Act when it passed the Senate.⁴⁰ Similarly, former Majority Leader Harry Reid attempted to legalize online poker via the failed \$1.1 trillion omnibus spending bill during the 2010 lame duck congressional session.⁴¹

In an effort to address concerns of Internet gambling opponents, H.R. 2267 would have amended Title 31 of the U.S. Code to allow for control of Internet gambling “by a strict Federal licensing and regulatory framework to protect underage and otherwise vulnerable individuals, to ensure the games are fair, to address the concerns of law enforcement, and to enforce any limitations on the activity established by the States and Indian tribes.”⁴² If ever enacted, Rep. Frank’s regulations would ensure that Internet gambling operators: 1) are in good legal and financial standing; 2) utilize technology to ensure that age and location requirements are met; 3) implement systems to protect minors and problem gamblers; and 4) implement methods to identify and combat money laundering, fraud and to protect the privacy and security of online gamblers.⁴³ The bill would also give the Treasury Secretary full regulatory authority over Internet gambling facilities, and states could provide regulatory and enforcement support.⁴⁴

The licensing, regulatory, and enforcement mechanisms are not as clear-cut as they may appear to be in the congressional proposals, however. Two key issues could easily complicate the scheme: extraterritorial gaming operations and the ability of states to opt out of the scheme. Whether a jurisdiction adopts a state monopoly approach or a licensing scheme in order to “regulate” the gaming and “tax” the gaming revenues of the operator, the enterprises will face competition from off-shore operators, who continue to offer Internet poker and other games using non-credit tools, such as debit and check collection systems that allow a player to stake money in a game. Even if the U.S. Department of Justice pursues such accounts that sit in the U.S. as proceeds of an activity that violates the Wire Act, the off-shore activity presents a relatively easy way around UIGEA, as the current level of on-line poker testifies.

Additionally, if a state-sponsored scheme requires considerable controls, checks, and other legal compliance measures on a player, the player may prefer the more free-wheeling participation in gaming with the off-shore operator. Also, the congressional proposals generally allow states to place additional regulatory measures or simply to “opt out,” in which case a domestic-licensed operator cannot take bets from players resident in that state. While respecting federalism, such a scheme may lead to a checkerboard of jurisdictional issues, inconsistent regulation, criminal and civil enforceability issues, and constitutional questions. On the other hand, a totally preemptive national gambling law for the Internet disrespects the states’ police powers in matters such as gambling, generally

recognized as a disfavored industry subject to the states' police powers.

In the interim, federal prosecutors continue to search for—and attempt to seize—cash sitting in accounts at domestic banks and financial institutions, belonging to payment processor firms servicing off-shore on-line poker operators, including those located in Isle of Man, Antigua, and Barbuda, and certain Canadian First Nations. Reflecting uncertainty about whether the federal Wire Act reaches the activity, federal prosecutors have, in some cases, relied upon the fact that the online gaming is illegal in the state in which the assets are sought to be seized.⁴⁵ The federal prosecutors appear to focus principally on anti-money laundering, as well as anti-terrorist concerns. Generally speaking, international cooperation on anti-money laundering efforts is generally robust, including participation in an international body, the Financial Action Task Force on Money Laundering (FATF) (Groupe d'action financière sur le blanchiment de capitaux (GAFI)), founded in 1989 by the G7. However, several small island nations, enclaves, and European principalities are not participants and typically do not require the same steps to be taken to prevent, detect, or report large fraudulent cash transfers, such as the use of Currency Transaction Reports (CTR) or Suspicious Activity Reports (SAR), measures required of U.S. financial institutions under the Bank Secrecy Act.⁴⁶ Of course, the proposals for legalized on-line gaming in the United States do require that all parties adopt strong anti-money laundering provisions, as well as other strong regulatory controls. It seems doubtful, however, if at least extremely difficult, that such provisions will reach extra-territorial jurisdictions that do not cooperate in internationally-approved anti-money laundering efforts.

Even with strong regulatory provisions, it is likely that the social costs associated with gambling will increase as gambling becomes more available. For example, studies indicate two to four percent of adults have a gambling problem.⁴⁷ Four to eight percent of adolescents have a very serious gambling problem, while another ten to fifteen percent are at-risk.⁴⁸ Researchers emphasize that the proximity of gambling can be a key factor in predicting greater risk for problems.⁴⁹ Because Internet gambling provides greater proximity than any other gambling venue, it heightens the inherent risks.⁵⁰

Even those not susceptible to developing a gambling problem are susceptible to the greater risk of fraud associated with Internet gambling. Because it is virtually unregulated, there is little opportunity for a player to know whether the games being played over the Internet are fixed.⁵¹ Over a decade ago the National Gambling Impact Study Commission reported that:

assessing the integrity of Internet operators is quite difficult. Background checks for licensing in foreign jurisdictions are seldom as thorough as they are in the United States. Furthermore, the global dispersion of Internet gambling operations makes the vigilant regulation of the algorithms of Internet games nearly impossible.⁵²

Risks include site operators defrauding customers, players cheating one another through collusion without the benefit of visual surveillance, and involvement of organized crime.⁵³

Recently, mainstream Internet poker sites have been forced to refund millions of dollars to players as a result of alleged cheating. Most troubling, was the Internet providers' lack of willingness to provide information to prosecutors and players.⁵⁴

Finally, the debate over authorizing Internet gambling in the United States raises issues that complicate tribal gaming. Tribes are authorized to conduct certain gaming activities under the Indian Gaming Regulatory Act of 1988.⁵⁵ In order to conduct games such as lotteries, casino-style games and pari-mutuel wagering, a tribe must negotiate a compact with the State in which it is located and provide for adequate regulation. Essentially, this is brick-and-mortar gambling, just on Indian lands. Gaming on the Internet presents all of the same questions of criminality, enforcement, and regulation on, as off, the reservation. A further complication is the inherent "exclusivity" of much Indian gaming, in which States have essentially granted a monopoly to tribes to conduct gaming not otherwise permitted within the State,⁵⁶ usually in return for a share of the gaming revenue. The national authorization of Internet gaming will effectively undercut much of the monopoly the tribes enjoy. Currently, tribes are split on the question, some suggesting they can and should capitalize on the venture, others concerned for their brick-and-mortar establishments.

As the debate over legalizing gambling on the Internet continues, we should be mindful of both the costs and benefits of gambling. While it can provide an increase in revenue and personal liberty, social costs will increase, including broken families, criminal activity, and cheating.

Endnotes

1 Liz Benston & Karoun Demirjian, *Harry Reid Rushes Effort to Legalize Internet Poker*, LAS VEGAS SUN, Dec. 7, 2010.

2 Internet Gambling Regulation, Consumer Protection, and Enforcement Act, H.R. 2267, 111th Cong. (2009). The "Internet Gambling Regulation, Consumer Protection, and Enforcement Act" passed out of committee 41-22. See H. COMM. ON FINANCIAL SERVICES, 111TH CONG., MARKUP ON H.R. 2267, INTERNET GAMBLING REGULATION, CONSUMER PROTECTION, AND ENFORCEMENT ACT (Comm. Print 2010), available at http://financialservices.house.gov/Media/file/markups/7_28_2010/2267_final_passage_roll%20call.pdf.

3 Of thirty-eight Democrats voting, all but only four voted aye; of twenty-six Republicans voting, seven voted aye, eighteen opposed. *Id.*

4 In some jurisdictions, the definition is broader and includes games of "skill or chance," and others distinguish between games where chance "predominates." See ARS § 13-3301.

5 The expression "throwing or rolling the bones" derives from the ancient practice of throwing ground animal ankle bones.

6 WILLIAM M. THOMPSON, GAMBLING IN AMERICA: AN ENCYCLOPEDIA OF HISTORY, ISSUES, AND SOCIETY, at x, xxvi (2001).

7 NATIONAL GAMBLING IMPACT STUDY COMMISSION REPORT 2-1 (1999).

8 *Clark v. Washington*, 25 U.S. 40 (1827).

9 *Champion v. Ames*, 188 U.S. 321 (1903); see also *Ex Parte Jackson*, 96 U.S. 727 (1877) (holding that Congress can exclude from the mail a letter concerning lotteries which have been authorized by State legislation because it could be "injurious to public morals").

10 18 U.S.C. § 1084(a).

11 *In re MasterCard Intern. Inc., Internet Gambling Litigation*, 313 F.3d

257, 263(5th Cir. 2002) (holding that the Wire Act's legislative history, relevant case law and plain reading indicate that it only applies to betting on sporting events or contests).

12 Illegal Gambling Business Act of 1970, P.L. 91-452, Title VIII, § 803(a), Oct. 15, 1970, 84 Stat. 922, codified at 18 U.S.C. §1955.

13 18 U.S.C. § 1955.

14 28 U.S.C. § 3702.

15 28 U.S.C. § 3704(a)(2)(B).

16 OFC Comm Baseball v. Markell, 579 F.3d 293 (3d Cir. 2009), where the Third Circuit held that Delaware could not allow betting on individual NFL games because "parlay" or bets on multiple games where the type of betting permitted at the time the legislation was enacted.

17 Patrick McGreevey, *California May Benefit from Legalizing Sports Betting, State Senator Says*, L.A. TIMES, Aug. 1, 2010; see also John Brennan, *N.J. Senate Panel OKs Bill on Sports Betting*, NORTHJERSEY.COM, Nov. 22, 2010 (New Jersey legislators have been pushing legislation that would allow sports wagering because they expect it to generate \$220 million in annual income), available at http://www.northjersey.com/news/politics/112210_NJ_Senate_to_consider_gambling_changes.html.

18 Eric Pfanner, *Europe Unleashes Online Gambling to Fill Coffers*, N.Y. TIMES, July 27, 2010, at B2.

19 Bob Hartman, *Internet Gambling Growth to Reach \$528 Billion by 2015*, CASINO GAMBLING WEB, Dec. 12, 2006, available at <http://www.casinogamblingweb.com/gambling-news/online-casino/internet-gambling-industry-growth-to-reach-528-billion-by-2015-20607.html>.

20 The Gambling Act 2005, c. 19 (Eng.).

21 Pfanner, *supra* note 18.

22 *Id.*

23 Justine Hunter, *B.C. Online Gambling Glitches Fixed?*, GLOBE & MAIL, Aug. 19, 2010, available at <http://www.theglobeandmail.com/news/national/british-columbia/bc-online-gambling-glitches-fixed/article1679018/>.

24 31 U.S.C. §§5361-5366.

25 *Id.* § 5362(10)(A).

26 *Id.* §§ 5362(1)(B) and (D).

27 *Id.* §§ 5362(E)(viii), (ix); § 5362(10)(B)(iii)(state); and §5362(10)(C)(iv)(tribal).

28 Interactive Media Entm't & Gaming Ass'n v. Attorney Gen. of the U.S., 580 F.3d 113 (3d Cir. 2009).

29 *Id.* at 116.

30 *Id.*

31 *Id.* at 118.

32 *Id.*

33 On April 15, 2011, the U.S. Attorney in Manhattan filed charges under UIGEA against several Internet poker companies doing business in the United States, as well as for conspiracy to commit bank and wire fraud, money laundering and illegal gambling offenses, alleging approximately \$3 billion in illegal proceeds. The United States also filed a civil complaint and a restraining order against multiple bank accounts utilized by the companies and their payment processors, but not against any players' accounts.

34 I. Nelson Rose, *Viewpoint: The Unlawful Internet Gambling Enforcement Act of 2006 Analyzed*, 10 GAMING L. REV. 537 (2006).

35 *Id.*

36 Brant M. Leonard, Note, *Highlighting the Drawbacks of the UIGEA: Proposed Rules Reveal Heavy Burdens*, 57 DRAKE L. REV. 515, 544 (2009).

37 Joseph M. Kelly, *Financial Transaction Providers Needn't Worry Too Much About Complying With UIGEA Rules*, 13 GAMING L. REV. & ECON. 196, 201 (2009).

38 *Interactive Media Entm't & Gaming Ass'n*, 580 F.3d at 116 ("The Act prohibits a gambling business from knowingly accepting certain financial

instruments from an individual who places a bet over the Internet if such gambling is illegal at the location in which the business is located or from which the individual initiates the bet. 31 U.S.C. §§ 5362(10)(A), 5363.").

39 Sewell Chan, *Congress Rethinks Its Ban on Internet Gambling*, N.Y. TIMES, July 29, 2010, at A1.

40 Security and Accountability for Every Port Act of 2006 (or SAFE Port Act), Pub.L. 109-347, Title VIII, § 801, (Oct. 13, 2006).

41 Karen Demirjian, *All Bets Off: Online Poker Bill Dealt Possible Death Blow*, LAS VEGAS SUN, Dec. 17, 2010.

42 31 U.S.C. §5381(3).

43 *Id.* §5381(5).

44 *Id.* §5383(a).

45 *Feds Quietly Freeze Online Poker Cash in Washington*, The Jungle, <http://blogs.forbes.com/nathanvardi> (Jan. 5, 2011, 8:43 EST), available at <http://blogs.forbes.com/nathanvardi/2011/01/05/feds-quietly-freeze-online-poker-cash-in-washington/>.

46 31 U.S.C. §§ 5311-5330 ; 31 C.F.R. § 103.

47 See MALCOLM K. SPARROW ET AL., CAN INTERNET GAMBLING BE EFFECTIVELY REGULATED? MANAGING THE RISKS 61 (2009).

48 Jeffery Derevensky & Rena Gupta, *Prevalence Estimates of Adolescent Gambling: A Comparison of the SOGS-RA, DSM-IV-J, and the GA. 20 Questions*, 16 J. OF GAMBLING STUD. 227 (2000); D. F. Jacobs, *Juvenile Gambling in North America: An Analysis of Long Term Trends and Future Prospects*, 16 J. OF GAMBLING STUD. 119 (2000).

49 Brian Rush et al., *Mapping the Prevalence of Problem Gambling and Its Association with Treatment Accessibility and Proximity to Gambling Venues*, 20 J. OF GAMBLING ISSUES 193 (2007).

50 See MARK GRIFFITHS ET AL., INTERNET GAMBLING: A SECONDARY ANALYSIS OF FINDINGS FROM THE 2007 BRITISH GAMBLING PREVALENCE SURVEY (2008). This study found that pathological gambling rates were greater among Internet gamblers than non-Internet gamblers.

51 See SPARROW, *supra* note 46, at 9-11.

52 NATIONAL GAMBLING IMPACT STUDY COMMISSION REPORT, *supra* note 7, at 5-6.

53 See SPARROW, *supra* note 46, at 3.

54 Gilbert M. Gaul, *Players Gamble on Honesty, Security of Internet Betting*, Wash. Post, Nov. 30, 2008, available at http://www.washingtonpost.com/wp-dyn/content/article/2008/11/29/AR2008112901679_pf.html.

55 Indian Gaming Regulatory Act, Pub. L. No. 100-497, 102 Stat. 2467 (1988) (codified as amended at 18 U.S.C. §§ 1166-1168 (2006) and 25 U.S.C. §§ 2701-2721 (2006)). For legislative background, see S. Rep. No. 100-446, at 1 (1988), reprinted in 1988 U.S.C.C.A.N. 3071, 3071-74.

56 See Kevin Gover & Tom Gede, *The States as Trespassers in a Federal-Tribal Relationship: A Historical Critique of Tribal-State Compacting under IGRA*, 42 ARIZ. ST. L.J. 185, 211 (2010).

