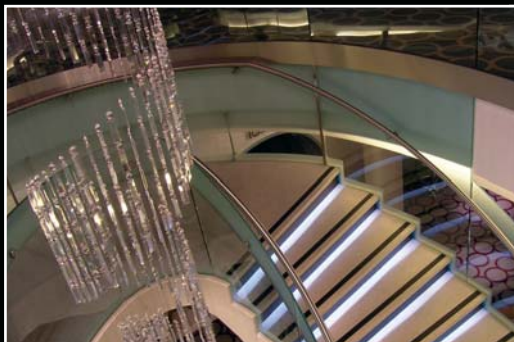




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MIRED BATTLES, BUT A WINNABLE WAR?

BY JOE KELLY AND FRANK CATANIA

Attempts at state and federal level to make inroads into the US Internet gambling ban, particularly in regard to poker, are proving arduous and drawn out. Despite a gathering momentum for change amid straightened economic circumstances, the prospects for the immediate future remain problematic. While the soundness of the regulatory case is being demonstrated more forcefully with every official rebuttal, the immediate future for legal online poker is not promising.



On 13th October 2006 the Unlawful Internet Gambling Enforcement Act (UIGEA) was enacted into law. It was attached to a totally unrelated bill and was not read by the vast majority of Members of Congress. UIGEA did not define what was unlawful Internet gambling, but its failure to apply the "predominant test" to games of skill disappointed both poker players and operators. Poker supporters were also disappointed when the regulatory authorities (the Treasury Department and the Federal Reserve System) rejected the "predominant test" for a skill game definition and instead used the test of whether chance was a "significant factor" in determining whether a game was an exempt game of skill. Non-exempt financial transaction providers were also required to finalise written policies concerning unlawful Internet gambling by 1st December 2009.

In 2009 a bill was introduced into the House of Representatives that would delay 1st December 2009 date. Massachusetts Democratic Representative Barney Frank and 18 other members of Congress have also written to the Treasury Department and Federal Reserve asking that the written policy compliance date be extended by one year, but it is doubtful whether regulators will be influenced by a letter-writing campaign.

The UIGEA might be modified by two very significant interactive gaming bills that were submitted to Congress in 2009. On 6th May 2009, Barney Frank introduced HR 2267 (48 pp) entitled "The Internet Gambling Regulation Consumer Protection and Enforcement Act of 2009", which presently has 62 co-sponsors. On 6th August 2009, New Jersey Democratic Senator Robert Menendez introduced S. 1597 entitled the "Internet Poker and Games of Skill Regulation, Consumer Protection and Enforcement Act of 2009". The 91-page bill presently has no co-sponsors.

The major difference between the bills is that the Frank bill would license and regulate all interactive gambling, except for sports betting, while the Menendez bill would license only non-banking interactive poker and other skill gambling as well as legalise interactive interstate horseracing "without need for a licence pursuant".

The Frank bill and the Menendez bill contain remarkably similar provisions. Both bills delegate enforcement responsibility to the Secretary of the Treasury (the Secretary) to develop regulations and a licensing framework within 180 days from passage of the bill in order to ensure that all respective licensees of Internet gaming facilities and games of skill are suitable, solvent, and willing to carry out socially responsible policies. The Secretary, upon determination of suitability, solvency, and social responsibility, would then issue five-year renewable licences to Internet gaming and game of skill operators.

Specifically, all gambling applicants would be required to submit, inter alia, "(A) The criminal and credit history of the applicant [and any senior officers]. (B) The financial statements of the applicant. (C) Documentation showing the corporate structure of the applicant and all related businesses and affiliates. (D) Documentation containing detained evidence of the applicant's plan for complying with all applicable regulations should a licence be issued, with particular emphasis on the applicant's ability" to (i) protect or prevent underage and problem gamblers and (ii) ensure games are being operated fairly.

Compliance with the above requirements would necessitate a thorough background check not only of the corporate applicant, but also the directors and senior executives of the business enterprise. The applicant would also be required to establish by the high evidentiary standard of "clear and convincing evidence" that the applicant "(A) is a person of good character, honesty and integrity;...(D) has or guarantees acquisition of adequate business competence and experience" in the operation of respective Internet gambling and games of skill facilities; and "(E) has or will obtain sufficient financing for the nature of the proposed operation and from a suitable source." Any conviction of an offence punishable by more than one-year's imprisonment, providing false information, or being delinquent in tax payments would automatically result in a determination of unsuitability.

Both bills would mandate the Secretary to require that the licensee has established mechanisms to ensure all bettors are in a jurisdiction that does not prohibit Internet gambling, that all gambling taxes are collected, that there are appropriate safeguards to prevent "fraud, money laundering, and terroristic finance" and to develop appropriate safeguards to prevent compulsive Internet gambling. The Secretary shall also have authority to examine all licensee records and require a licensee to attend a hearing. Should a licensee commit a willful violation of regulations, the licensee would be subject to a civil penalty not to exceed \$100,000.

The Secretary would also be authorised to defer determination as to the suitability of an applicant to a state or tribal regulatory body, although "the Secretary retains the authority to review, withhold, or revoke any licence if the Secretary has reason to believe that any applicant or licensee does not meet the suitability requirements for licensing established under this section, or any other requirement of a licensee." The Secretary could also rely on "qualified" state or tribal regulatory bodies "for such other regulatory and

enforcement activities" as the Secretary might find appropriate.

About seven pages of each bill are devoted to provisions mandating Responsible Gambling procedures, including a "Self-Exclusion Programme". Among the minimum requirements for such procedures are provisions ensuring that customers may establish loss limits, have access to responsible gambling material, and forfeiture by a self-excluded gambler of any winnings should the gambler ignore the self-exclusion. The Menendez bill would also require licensed operators "to prevent persons" on the self-excluded list from initiating wagers. The Menendez bill also authorised a study concerning the identification, prevention and treatment of problem gambling and to conduct a national campaign on problem gambling awareness issues. (Title III)

Both bills address the concerns of those states or tribes that do not want their residents to participate in US licensed online gambling. For example, the Governor or principle tribal chief may decide to opt out of any gaming inclusion within 90 days after the enactment of either bill.

There are certain differences between the bills. While the Frank bill is silent on taxation, its companion bill "The Internet Gambling Regulatory and Tax Enforcement Act of 2009" (HR2268), introduced by Washington Democratic Representative Jim McDermott, would establish a monthly two percent tax on all customer deposited Internet gambling funds. There is also a penalty of 50 percent of all deposited money should the gambling operator not be licensed. The licensed operator must also establish procedures for the reporting and taxing of customer winnings.

The Menendez bill (Title II, Internet Games of Skill Tax Provisions) would amend the Internal Revenue Code of 1986 to require a 10 percent gaming licensing fee on a "licensee's Internet gaming deposited funds for a calendar month". The amount would be split between the federal government and either the state or tribal government of the player. The Menendez bill also imposes huge tax penalties on an unlicensed operator, and a withholding tax on non-resident Aliens.

The Menendez bill also imposes a 21-year age requirement while the Frank bill defers to the legal age "as defined by state or tribal law". While both bills permit civil monetary and mandate user fees on licensed operators, the Frank bill makes both assessments "unappealable" while the Menendez bill permits judicial review of both the amount of the user fee and the appropriateness of the penalty.

Perhaps more significantly, the Menendez bill specifically states that an online skill gaming operator who had accepted US players could not be denied a licence for that reason, and could continue to accept customers while the application was pending. The Frank bill would deny a licence to a gaming applicant that had been convicted of an offence with a one-year imprisonment penalty, but is unclear as to the licensing prospects of a non-sports gaming operator who accepted US customers. The Menendez bill, unlike the Frank bill, would not defer to a state or tribal gaming determination on suitability unless the regulations were "no less stringent" than those that would be established by the Secretary.

Finally, the Menendez bill would require the Director of the Financial Crime Enforcement Network (FinCen) to draft a list of unlawful Internet gambling enterprises, including the names of owners and financial agents (Sec 103). Should the Director include an enterprise, it would then be the burden of

the operator to establish "by a preponderance of the evidence that such a person is not an unlawful Internet gambling enterprise" before the federal court of the District of Columbia.

It is widely believed that the Frank bill will be the first to move through Congress, but probably not until 2010. It is uncertain whether the Menendez bill will divide the online gambling licensing supporters since the major hurdle for any bill seems to be proving to members of Congress that regulated internet gaming can verify both the location of the player and the minimum age requirement through a "know your customer" policy. These verification procedures should be the same for all interactive gambling.

For a time, it appeared that the Menendez bill would receive a big boost when Oregon Democratic Senator Ron Wyden considered proposing an amendment to Senator Max Baucus' health care bill that would have designated a portion of Internet gambling proceeds to health insurance subsidies for low income US residents. Several days later, Senator Wyden withdrew the amendment because "the last thing Senator Wyden wants to do is make it more difficult to expand subsidies for working families by introducing a new contentious issue to the debate," said Jennifer Hoelzer, his communications director. So when he offers the amendment, he will do it with other funding mechanisms." For online poker, Wyden's withdrawal was especially frustrating since the amendment might have resulted in favourable publicity within the US Senate where Nevada Democratic Majority Leader Harry Reid has been previously negative regarding any online gaming regulation.

At the state level, online poker advocates have had little to cheer about. California had seemed ready to embrace an intrastate online poker bill, especially since it was doubtful that the Obama administration, unlike its predecessor, would interfere in intrastate activity. In August 2009, the powerful Morongo Indian Tribe had suggested an intrastate poker bill that would have created a new corporation consisting of tribal casinos and legal poker card clubs that would develop intrastate online poker. It is undisputed that the bill would have raised hundreds of millions, perhaps \$450 million, for cash strapped California. Tribal and other opposition, however, delayed introduction of any bill until 2010. Florida has authorised a feasibility study, due 1st December 2009, as to whether Internet poker can be effectively regulated. It is doubtful whether any legislative action will be taken until the Seminole compact issues are resolved.

A second major disappointment occurred in Massachusetts where the Attorney General rejected a proposed referendum on the state ballot to legalise intrastate Internet poker as long as the site and payment providers were state approved. The bill's major sponsor, the Poker Players Alliance, had stressed the revenue that would be raised by legalising intrastate online poker. The Attorney General opined that the proposal was ambiguous. "We simply cannot determine whether, if the proposed law were enacted, any financial services providers would be required to make the five percent payment to the Commonwealth [of Massachusetts]."

It was also discouraging to poker players that the Court of Appeals in the state of Washington upheld an absurd law that makes online gambling including poker a class C felony which is the same as rape. This statute and decision would have been considered bizarre even in 18th Century London.

The only bright spot is that the Washington Supreme Court has agreed to review this highly unusual decision.

For now the immediate future of legal online poker in the US does not seem promising. Governments will continue to lose valuable revenue by not licensing, regulating and taxing a popular game which has minimal negative consequences. Prohibition, as in the 1920's liquor experiment, has not worked and will only encourage widespread disobedience of this unenforceable law. **CGI**

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JOE KELLY AND FRANK CATANIA



Joseph M. Kelly, Ph.D., J.D., is a Professor of Business Law at State College at Buffalo, and an associate of the Catania Consulting Group of New Jersey, specialising in gaming matters. He is licensed to practice law in Illinois, Nevada and Wisconsin.

Joe is co-editor of the *Gaming Law Review and Economics*, a leading gaming law journal. He is considered an expert in the field of gaming, having lectured on various gaming topics worldwide. His law review publications have been cited as authority by federal and state courts in the United States.

Joe has been used as an expert witness for several gaming companies, the United States Virgin Islands Casino Control Commission, the South African Parliamentary Committee on Trade and Industry ,Antigua and Barbuda and as an expert on poker in the trial of R v Kelly (Gutshot)(2007) in Crown Court (London), UK. He was also the major speaker on poker law at the Barcelona conference of the International Association of Gaming Regulators in 2006



Frank Catania is a senior partner in Catania Gaming Consultants and the Law Firm of Catania Ehrlich & Suarez of New Jersey, both having extensive experience in gaming related matters. He is the former Director of the New Jersey Division of Gaming

Enforcement, serves as an independent director of eCOGRA, Nevada Gold Casinos and Continent 8. He is a member and served as the first president of the International Masters of Gaming Law. Frank has been published on a wide variety of casino gaming and government-related topics in several national publications, regional newspapers, and trade publications. He was instrumental in drafting gaming regulations for several gaming jurisdictions. Frank has been an advocate for regulation of Internet gaming in the United States.