

Unlawful Internet Gambling Enforcement Act (UIGEA) and Its Implementing Regulations

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Summary

The Unlawful Internet Gambling Enforcement Act (UIGEA) seeks to cut off the flow of revenue to unlawful Internet gambling businesses. It outlaws receipt of checks, credit card charges, electronic funds transfers, and the like by such businesses. It also enlists the assistance of banks, credit card issuers and other payment system participants to help stem the flow of funds to unlawful Internet gambling businesses. To that end, it authorizes the Treasury Department and the Federal Reserve System (the Agencies), in consultation with the Justice Department, to promulgate implementing regulations. The Agencies adopted a final rule implementing the provisions of the UIGEA, 73 *Fed. Reg.* 69382 (November 18, 2008); the rule was effective January 19, 2009, with a compliance date of June 1, 2010.

The final rule addresses the feasibility of identifying and interdicting the flow of illicit Internet gambling proceeds in five payment systems: card systems, money transmission systems, wire transfer systems, check collection systems, and the Automated Clearing House (ACH) system. It suggests that, except for financial institutions that deal directly with illegal Internet gambling operators, tracking the flow of revenue within the wire transfer, check collection, and ACH systems is not feasible at this point. It therefore exempts them from the regulations' requirements. It charges those with whom illegal Internet gambling operators may deal directly within those three systems, and participants in the card and money transmission systems, to adopt policies and procedures to enable them to identify the nature of their customers' business, to employ customer agreements barring tainted transactions, and to establish and maintain remedial steps to deal with tainted transactions when they are identified. The final rule provides non-exclusive examples of reasonably designed policies and procedures to prevent restricted transactions. The rule also explains why the Agencies rejected a check-list-of-unlawful-Internet-gambling-operators approach, asserting that such a list of businesses would not be practical, efficient, or effective in preventing unlawful Internet gambling. Rather, the Agencies argued that flexible, risk-based due diligence procedures conducted by participants in the payment systems, in establishing and maintaining commercial customer relationships, is the most effective method to prevent or prohibit the restricted transactions.

Some Members of Congress have criticized the current Internet gambling restrictions for being, in their view, ineffective at stopping Internet gambling, an infringement on individual liberty, and a lost opportunity to collect tax revenue, among other things. The 111th Congress has held several hearings concerning legislative proposals to loosen the current restrictions on Internet gambling activities. The bill with the most action to date has been H.R. 2267 (Internet Gambling Regulation, Consumer Protection, and Enforcement Act), which would establish a licensing program under which Internet gambling companies may lawfully operate and accept bets or wagers from individuals located in the United States. The House Financial Services Committee marked up and approved H.R. 2267 on July 29, 2010. A companion bill to H.R. 2267 is H.R. 4976 (Internet Gambling Regulation and Tax Enforcement Act of 2010), which would establish a licensing fee regime within the Internal Revenue Code for Internet gambling operators. S. 1597 (Internet Poker and Game of Skill Regulation, Consumer Protection, and Enforcement Act of 2009) would create a federal licensing program somewhat similar to that of H.R. 2267, except that the permitted Internet gambling operations would be limited to those that offer online games "in which success is predominantly determined by the skill of the players, including poker, chess, bridge, mah-jong, and backgammon."

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Background

Passage of the Unlawful Internet Gambling Enforcement Act (UIGEA) in 2006 as Title VIII of the SAFE Port Act[1] represented the culmination of legislative consideration that began with the recommendations of the National Gambling Commission.[2]

UIGEA prohibits gambling-related businesses from accepting checks, credit card charges, electronic transfers, and similar payments in connection with unlawful Internet gambling.[3] Anyone who violates this prohibition of UIGEA is subject to a criminal fine of up to $250,000 (or $500,000 if the defendant is an organization), imprisonment of up to five years, or both.[4] In addition, upon conviction of the defendant, the court may enter a permanent injunction enjoining the defendant from making bets or wagers "or sending, receiving, or inviting information assisting in the placing of bets or wagers."[5] The Attorney General of the United States or a state attorney general may bring civil proceedings to enjoin a transaction that is prohibited under UIGEA.[6]

As a consequence of UIGEA and Department of Justice enforcement efforts, NETeller, which reportedly processed more than $10 billion in gambling proceeds between U.S. customers and offshore Internet gambling business from 1999 to 2007, entered into a deferred prosecution agreement under which it agreed to discontinue U.S. operations, cooperate with investigators, and to pay the U.S. $136 million in sanctions and to return an additional $96 million to U.S. customers.[7] Several offshore Internet gambling companies have apparently sought similar agreements.[8] A number of large banking institutions, which underwrote the initial public offers for offshore Internet gambling companies on the London stock exchange, have been the targets of grand jury subpoenas as well.[9]

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[1] P.L. 109-347, 120 Stat. 1952 (31 U.S.C. 5361-5367) (2006).

[2] National Gambling Impact Study Commission, *Final Report* at 5-12 (1999). Earlier related CRS Reports include CRS Report RS22418, *Internet Gambling: Two Approaches in the 109th Congress*, from which some of this report is drawn, and CRS Report RS21487, *Internet Gambling: A Sketch of Legislative Proposals in the 108th and 109th Congresses*, which includes a more extensive discussion of the legislation's evolution.

[3] 31 U.S.C. § 5363. UIGEA's prohibition applies to anyone "engaged in the business of betting or wagering;" however, it expressly excludes from the definition of the term "business of betting or wagering" the services of a financial intermediary or Internet service provider that may be used in connection with the unlawful bet. 31 U.S.C. § 5362(2); *see* Interactive Media Entm't & Gaming Ass'n v. AG of the United States, 2009 U.S. App. LEXIS 19591, *2-3 n.1 (3d Cir. 2009).

[4] 31 U.S.C. § 5366(a).

[5] 31 U.S.C. § 5366(b).

[6] 31 U.S.C. § 5365.

[7] "Neteller to Pay Dollars 136m Gambling Penalty," *Financial Times USA* at 16 (July 19, 2007).

[8] *Id.*; "Sportingbet Cuts Deal," *Express on Sunday* at 7 (August 5, 2007) ("Sportingbet is now following the lead of rivals PartyGaming and 888 Holdings which started talks with the United States Attorney's Office ... in a bid to remove the threat of any criminal proceedings."); Eric Pfanner, "A New Chance for Online Gambling in the U.S.," *New York Times* (April 27, 2009) ("This month, PartyGaming agreed to a $105 million settlement with the U.S. attorney's office in New York, involving the period before 2006, when it acknowledged that its activities had been 'contrary to certain U.S. laws.' In turn, the U.S. authorities agreed not to prosecute the company, which is listed on the London Stock Exchange, or its executives.").

[9] Andrew Ross Sorkin and Stephanie Saul, "Gambling Subpoenas on Wall St," *New York Times,* at C1 (January 22, 2007).

UIGEA's definition of "unlawful Internet gambling" does not specify what gambling activity is illegal; rather, the statute relies on underlying federal or state gambling laws to make that determination:

> The term "unlawful Internet gambling" means to place, receive, or otherwise knowingly transmit a bet or wager by any means which involves the use, at least in part, of the Internet where such bet or wager is unlawful under any applicable Federal or State law in the State or Tribal lands in which the bet or wager is initiated, received, or otherwise made.[10]

However, this statutory definition expressly *exempts* lawful intrastate and intratribal Internet gambling operations that feature age and location verification requirements imposed as a matter of law.[11] UIGEA further defines the term "bet or wager" to mean "the staking or risking by any person of something of value upon the outcome of a contest of others, a sporting event, or a game subject to chance, upon an agreement or understanding that the person or another person will receive something of value in the event of a certain outcome."[12] The statutory definition includes lottery participation, gambling on athletic events, and information relating to financing a gambling account, but a "bet or wager" does *not* include the following:

- securities transactions;
- commodities transactions;
- over-the-counter derivative instruments;
- indemnity or guarantee contracts;
- insurance contracts;
- bank transactions (transactions with insured depository institutions);
- games or contests in which the participants do not risk anything but their efforts; or
- certain fantasy or simulation sports contests.[13]

UIGEA leaves in place questions as to the extent to which the Interstate Horseracing Act curtails the reach of other federal laws,[14] an issue that was at the center of World Trade Organization (WTO) litigation.[15] The statute instructs the Secretary of the Treasury and the Board of Governors

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[10] 31 U.S.C. § 5362(10)(A).

[11] 31 U.S.C. § 5362(10)(B), (C) (The state law or regulation, or tribal ordinance, resolution, or tribal-state compact, must include "age and location verification requirements reasonably designed to block access to minors and persons located" out of such state or out of the applicable tribal lands.).

[12] 31 U.S.C. § 5362(1)(A).

[13] 31 U.S.C. § 5362(1)(B)-(E).

[14] 31 U.S.C. § 5362(10)(D)(iii). The Justice Department and certain members of the horse racing industry disagree over the extent to which the Horseracing Act amends the coverage of the Wire Act that outlaws the interstate transmission by wire of certain information related to gambling. UIGEA denies that its provisions are intended to resolve the dispute.

[15] *See e.g.*, *Don't Bet on the United States's Internet Gambling Laws: The Tension Between Internet Gambling Legislation and World Trade Organization Commitments*, 2007 COLUMBIA BUSINESS LAW REVIEW 439. In the WTO dispute, Caribbean nation Antigua and Barbuda ("Antigua") argued that the United States discriminates against foreign Internet gambling operators while permitting domestic, online gambling on horse racing, in violation of U.S. market access commitments under the General Agreement on Trade in Services treaty. Antigua won its case before the WTO, and on December 21, 2007, a WTO arbitration report determined that Antigua had suffered $21 million in damages (continued...)

of the Federal Reserve, in consultation with the Attorney General, to issue implementing regulations within 270 days of passage.[16]

On September 1, 2009, a federal appeals court ruled that UIGEA is not unconstitutionally vague.[17] The Interactive Media Entertainment & Gaming Association had filed a lawsuit alleging that UIGEA was facially unconstitutional, and sought to enjoin the enforcement of the act and its regulations. The U.S. Court of Appeals for the Third Circuit disagreed with Interactive's assertion that UIGEA was void for vagueness because of the lack of an "ascertainable and workable definition" of the statutory phrase "unlawful Internet gambling":

> The Supreme Court has explained that a statute is unconstitutionally vague if it "fails to provide a person of ordinary intelligence fair notice of what is prohibited, or is so standardless that it authorizes or encourages seriously discriminatory enforcement." United States v. Williams, 128 S. Ct. 1830, 1845, 170 L. Ed. 2d 650 (2008).... We reject Interactive's vagueness claim. 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. Thus, the Act clearly provides a person of ordinary intelligence with adequate notice of the conduct that it prohibits.[18]

The appellate court noted that UIGEA "itself does not make any gambling activity illegal," but rather, the definition of "unlawful Internet gambling" references federal and state laws related to gambling.[19] Therefore, the court suggested that "to the extent that [there is] a vagueness problem, it is not with the Act, but rather with the underlying state law."[20]

Regulations Implementing UIGEA

UIGEA calls for regulations that require "each designated payment system, and all participants therein, to identify and block or otherwise prevent or prohibit restricted transactions through the establishment of policies and procedures" reasonably calculated to have that result, 31 U.S.C. 5364(a). On October 4, 2007, the Board of Governors of the Federal Reserve System and the Treasury Department (the Agencies) issued proposed regulations implementing UIGEA, 72 *Fed. Reg.* 56680. The proposal invited commentators to suggest alternatives and critiques before the close of the comment period on December 12, 2007. The proposal offered to exempt substantial activities in those payment systems in which tracking is not possible now and in which it may

(...continued)

annually. The WTO arbitrator ruled that Antigua may request authorization to suspend a maximum of $21 million annually in obligations owed to the United States under the WTO Agreement on Trade-Related Aspects of Intellectual Property Rights. (In other words, Antigua could infringe the rights of U.S. holders of copyrights, trademarks, and patents, up to $21 million a year.) Decision by the Arbitrator, Recourse to Arbitration by the United States for Arbitration under Article 22.6 of the DSU, United States—Measures Affecting the Cross-Border Supply of Gambling and Betting Services, WT/DS285/ARB (December 21, 2007). For more information on this case, *see* CRS Report RL32014, *WTO Dispute Settlement: Status of U.S. Compliance in Pending Cases*, by Jeanne J. Grimmett.

[16] 31 U.S.C. § 5364.

[17] Interactive Media Entm't & Gaming Ass'n v. AG of the United States, 2009 U.S. App. LEXIS 19591 (3d Cir. 2009).

[18] *Id.* at *7.

[19] *Id.* at *11-12.

[20] *Id.* at *11.

ultimately not be feasible. It also noted that the two Agencies felt that they have no authority to compel payment system participants to serve lawful Internet gambling operators.[21] After taking into consideration the public comments on the proposed rule and consulting with the Department of Justice (as required by the UIGEA), the Agencies adopted a final rule implementing the provisions of the UIGEA, 73 *Fed. Reg.* 69382 (November 18, 2008); the rule was effective January 19, 2009, with a compliance date of June 1, 2010 (originally December 1, 2009).[22]

Designated Payment Systems & Due Diligence

The final rule identifies five relevant payment systems that could be used in connection with, or to facilitate, the "restricted transactions" used for Internet gambling: Automated Clearing House System (ACH), card systems, check collection systems, money transmitting business, and wire transfer systems, new 31 C.F.R. §132.3. The rule defines a "restricted transaction" to mean any transactions or transmittals involving any credit, funds, instrument, or proceeds that the UIGEA prohibits any person engaged in the business of betting or wagering from knowingly accepting, in connection with the participation of another person in unlawful Internet gambling, new 31 C.F.R. §132.2(y). However, the rule does *not* provide a more specific definition of the term "unlawful Internet gambling;" instead, it restates the UIGEA's definition.[23]

While the Agencies expect that card systems will find that using a merchant and transaction coding system is "the method of choice" to identify and block restricted transactions, the Agencies felt that the most efficient way for other designated payment systems to comply with the UIGEA is through "adequate due diligence by participants when opening accounts for commercial customers to reduce the risk that a commercial customer will introduce restricted transactions into the payment system in the first place," 73 *Fed. Reg.* 69394 (November 18, 2008).

The rule directs participants in the designated systems, unless exempted, to "establish and implement written policies and procedures reasonably designed to identify and block or otherwise prevent or prohibit restricted transactions," new 31 C.F.R. §132.5(a), and then provides non-exclusive examples of reasonably compliant policies and procedures for each system, new 31 C.F.R. §132.6. Participants may comply by adopting the policies and procedures of their payments system or by adopting their own, new 31 C.F.R. §§132.5(b), 132.6(a). Participants that establish and implement procedures for due diligence of their commercial customer accounts or commercial customer relationships will be considered in compliance with the regulation if the procedures include the following steps, new 31 C.F.R. § 132.6(b):

1. At the establishment of the account or relationship, the participant conducts due diligence of a commercial customer and its activities commensurate with the

[21] "Some payment system operators have indicated that, for business reasons, they have decided to avoid processing any gambling transactions, even if lawful, because among other things, they believe that these transactions are not sufficiently profitable to warrant the higher risk they believe these transactions pose." The Agencies do not believe UIGEA authorizes them to countermand such a decision, 72 *Fed. Reg.* 56688 (October 4, 2007).

[22] The original compliance date of December 1, 2009, was extended by six months by order of the Department of the Treasury and the Federal Reserve Board, in response to a petition submitted by three gambling industry associations that were concerned that many small regulated entities did not have the resources necessary to develop and implement appropriate policies and procedures by the compliance date, 74 *Fed. Reg.* 65687 (Dec. 1, 2009).

[23] 31 C.F.R. § 132.2(bb).

participant's judgment of the risk of restricted transactions presented by the customer's business.

2. Based on its due diligence, the participant makes a determination regarding the risk the commercial customer presents of engaging in an Internet gambling business. Such a determination may take one of the two courses set forth below:

    a. The participant determines that the commercial customer presents a minimal risk of engaging in an Internet gambling business (such as commercial customers that are directly supervised by a federal functional regulator,[24] or an agency, department, or division of the federal government or a state government), or

    b. The participant cannot determine that the commercial customer presents a minimal risk of engaging in an Internet gambling business, in which case it must obtain a certification from the commercial customer that it does not engage in an Internet gambling business. If the commercial customer does engage in an Internet gambling business, the participant must obtain: (1) documentation that provides evidence of the customer's legal authority to engage in the Internet gambling business and a written commitment by the commercial customer to notify the participant of any changes in its legal authority to engage in its Internet gambling business, and (2) a third-party certification that the commercial customer's systems for engaging in the Internet gambling business are reasonably designed to ensure that the commercial customer's Internet gambling business will remain within the licensed or otherwise lawful limits, including with respect to age and location verification.

3. The participant notifies all of its commercial customers that restricted transactions are prohibited from being processed through the account or relationship, "through a term in the commercial customer agreement, a simple notice sent to the customer, or through some other method, "73 *Fed. Reg.* 69393 (November 18, 2008).

Non-exclusive Examples of Compliant Policies and Procedures

Of the five payment systems, a "card system" as understood by the regulations is one that settles transactions involving credit card, debit card, pre-paid card, or stored value product and in which the cards "are issued or authorized by the operator of the system and used to purchase goods or services or to obtain a cash advance," new 31 C.F.R. §132.2(f). Merchant codes are a standard feature of the system which permits the system to identify particular types of businesses, 71 *Fed. Reg.* 56684 (October 4, 2007). There are no card system exemptions from the regulations' requirements. Examples of reasonably compliant policies and procedures feature due diligence and prophylactic procedural components. The standards involve screening merchants to determine the nature of their business, a clause prohibiting restricted transactions within the

[24] The term "federal functional regulator" means—the Board of Governors of the Federal Reserve System; the Office of the Comptroller of the Currency; the Board of Directors of the Federal Deposit Insurance Corporation; (D) the Director of the Office of Thrift Supervision; (E) the National Credit Union Administration Board; and (F) the Securities and Exchange Commission. 15 U.S.C. § 6809.

merchant agreement, as well as maintaining and monitoring a business coding system to identify and block restricted transactions, new 31 C.F.R. §132.6(d).

"Money transmitting businesses" are entities such as Western Union and PayPal that are in the business of transmitting funds, 71 *Fed. Reg.* 56684 (October 4, 2007). They too are without exemption from the UIGEA implementing regulations. Examples of acceptable policies and procedures for money transmitting businesses feature procedures to identify the nature of a subscriber's business, subscriber agreements to avoid restricted transactions, procedures to check for suspicious payment patterns, and an outline of remedial actions (access denial, account termination)[25] to be taken when restricted transactions are found, new 31 C.F.R. §132.6(f).

The regulations contain exemptions in varying degrees for the other payment systems. In essence, because of the difficulties of identifying tainted transactions, they limit requirements to those who may deal directly with the unlawful Internet gambling businesses. In the case of "check collection systems," the coded information available to the system with respect to a particular check is limited information identifying the bank and account upon which the check is drawn, and the number and amount of the check, 72 *Fed. Reg*. 56687 (October 4, 2007). Information identifying the payee is not coded and a "requirement to analyze each check with respect to the payee would substantially ... reduce the efficiency of the check collection system," 72 *Fed. Reg*. 56687 (October 4, 2007). Consequently, the final rule exempts all participants in a particular check collection through a check collection system except for "the first U.S. institution to which a check is transferred, in this case the institution receiving the check deposit from the gambling business," 72 *Fed. Reg*. 56687 (October 4, 2007)—namely, the depositary bank, new 31 C.F.R. §132.4(b).

Banks in which a payee deposits a check are covered by the regulations as are banks which receive a check for collection from a foreign bank. The rule offers examples for both circumstances. In the case of a check received from a foreign bank, examples of a depositary bank's reasonably compliant policies and procedures are procedures to inform the foreign banking office after the depositary bank has actual knowledge[26] that the checks are restricted transactions (such actual knowledge being obtained through notification by a government entity such as law enforcement or a regulatory agency), new 31 C.F.R. §132.6(e)(2). In the purely domestic cases, examples of reasonably compliant policies and procedures would include (1) due diligence in establishing and maintaining customer relations sufficient to identify the nature of a customer's business, and to provide for a prohibition on tainted transactions in the customer agreement, and (2) remedial action (refuse to deposit a check; close an account) should a tainted transaction be unearthed, new 31 C.F.R. §132.6(e)(1).

"Wire transfer systems" come in two forms. One involves large volume transactions between banks; the second, customer-initiated transfers from one bank to another, 72 *Fed. Reg*. 56685 (October 4, 2007). Like the check collection systems, under current practices only the recipient bank is in a realistic position to determine the nature of the payee's business. The Agencies sought public comments on whether additional safeguards should be required of the initiating

[25] However, "[a]s the examples in the rule are non-exclusive, a system or participant may choose to include fines in its policies and procedures where appropriate." 73 *Fed. Reg*. 69393 (November 18, 2008).

[26] "Actual knowledge" is defined by the regulation to mean, with respect to a transaction or commercial customer, "when a particular fact with respect to that transaction or commercial customer is known by or brought to the attention of (1) an individual in the organization responsible for the organization's compliance function with respect to that transaction or commercial customer, or (2) an officer of the organization." 31 C.F.R. § 132.2(a).

bank in such cases, 72 Fed. Reg. 56687 (October 4, 2007), but ultimately decided to exempt all but the bank receiving the transfer, new 31 C.F.R. §132.4(d).

Banks that receive a wire transfer (the beneficiary's bank) are covered by the regulations, and examples of reasonably compliant policies and practices resemble those provided for check collection system participants: know your customer, have a no-tainted transaction customer agreement clause, and have a remedial procedure (transfer denied; account closed) when tainted transactions surface, new 31 C.F.R. §132.6(g).

The "Automated Clearing House System" (ACH) is a system for settling batched electronic entries for financial institutions. The entries may be recurring credit transfers such as payroll direct deposit payments or recurring debit transfers such as mortgage payments, 72 *Fed. Reg*. 56683 (October 4, 2007). The entries may also include one time individual credit or debit transfers, *Id.* Banks periodically package credit and debit transfers and send them to a ACH system operator who sorts them out and assigns them to the banks in which the accounts to be credited or debited are found, *Id.* Participants are identified not according to whether they are transferring credits or debits but according to which institution initiated the transfer, i.e. originating depository financial institutions (ODFI) and receiving depository financial institutions (RDFI), *Id.*

The final rule exempts all participants processing a particular transaction through an ACH system, except for the RFDI in an ACH credit transaction, the ODFI in an ACH debit transaction, and the receiving gateway operator that receives instructions for an ACH debit transaction directly from a foreign sender, new 31 C.F.R. §132.4(a). These entities are not exempt under the theory that in any tainted transaction they will be in the best position to assess the nature of the business of the beneficiary of the transfer and to identify and block transfers to unlawful Internet gambling operators, 72 *Fed. Reg*. 56686 (October 4, 2007). The ACH system operator, ODFIs in a credit transaction and RDFIs in a debit transaction are exempt from the regulations, however, *Id.*

The examples of ACH system reasonably compliant policies and procedures are comparable to those for check collection and wire transfer systems: in purely domestic cases, know your customer, have a no-tainted transaction customer agreement clause, have a remedial procedure (disallow origination of ACH debit transactions; account closed) when tainted transactions surface; in the case of receiving transfers from overseas, know your foreign gateway operator, have a no-tainted transaction agreement, have a remedial procedure (ACH services denied; termination of cross-border relationship) when tainted transactions surface, new 31 C.F.R. §132.6(c). The Agencies explained that U.S. participants processing *outbound* cross-border credit transactions (ACH credits and wire transfers) are exempted "because there are no reasonably practical steps that a U.S. participant could take to prevent their consumer customers from sending restricted transactions cross-border," 73 *Fed. Reg.* 69389 (November 18, 2008). The Agencies explained that there is insufficient information to allow U.S. participants to identify and block restricted transactions in cross-border ACH credit transactions and sending wire transfers abroad, *Id.*

Unlawful Internet Gambling Operators Watch List

In the proposed regulations, the Agencies had explained why they did not follow a list-of-unlawful-Internet-gamblers approach similar to that used to deny drug dealers and terrorists access to American financial services (such as those administered by the Office of Foreign Assets Control (OFAC)), 72 *Fed. Reg*. 56690 (October 4, 2007).

The OFAC system is a product of the International Economic Emergency Powers Act (IEEPA) which grants the President extraordinary powers to deal with foreign threats to the national security, foreign policy or economy of the United States.[27] The Presidents have exercised their powers under IEEPA to bar financial dealings with various identified drug dealers and terrorists among others.[28] OFAC maintains an online list of the dealers and terrorists subject to the freeze.[29] It might be thought that assembling a list of known unlawful Internet gambling operators and their fiscal accomplices might work just as well.

After considering the public comments on this issue, the Agencies concluded that maintaining such a list would be a time-consuming effort for which they lack the expertise, and they also questioned its effectiveness, 73 *Fed. Reg.* 69384 (November 18, 2008). The Agencies provided several reasons to support their position that the watch list would be inefficient and ineffective in preventing unlawful activity:

- Because the UIGEA does not precisely define what activities constitute unlawful Internet gambling, but rather refers to activities that are illegal under various federal or state gambling laws, creating such a list would require the Agencies to interpret those laws in a way that might "set up conflicts or confusion with interpretations by the entities that actually enforce those laws."
- The payment transactions may not necessarily be made payable to the business's listed name.
- The list might become quickly outdated to the extent that Internet gambling businesses could quickly change their payments information to evade the law.

Legislation in the 111th Congress

Several bills have been introduced in the 111th Congress that would liberalize federal online gambling laws, two of which have been the subject of congressional hearings.[30] Such legislative proposals have been supported by Members of Congress who have criticized the current Internet gambling restrictions for being, in their view, ineffective at stopping Internet gambling by millions of Americans,[31] an infringement on individual liberty,[32] and a lost opportunity to collect billions of dollars in tax revenue,[33] among other things.

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[27] 50 U.S.C. §§ 1701-1707.

[28] *See e.g.*, E.O. 12978, Blocking Assets and Prohibiting Transactions With Significant Narcotics Traffickers, 60 *Fed. Reg.* 54579 (October 21, 1995); E.O. 13219, Blocking Property of Persons Who Threaten International Stabilization Efforts in the Western Balkans, 66 *Fed. Reg.* 34777 (June 26, 2001).

[29] 31 C.F.R. ch.V, App.A (July 1, 2006), available on November 1, 2007 at http://www.treasury.gov/offices/enforcement/ofac/sdn/t11sdn.pdf.

[30] *Tax Proposals Related to Legislation to Legalize Internet Gambling: Hearing Before the House Comm. on Ways and Means,* 111th Cong., 2nd sess. (2010); *H.R. 2267, Internet Gambling Regulation, Consumer Protection, and Enforcement Act: Hearing Before the House Comm. on Financial Services,* 111th Cong., 2nd sess. (2010).

[31] *Tax Proposals Related to Legislation to Legalize Internet Gambling: Hearing Before the House Comm. on Ways and Means,* 111th Cong., 2nd sess. (2010) (statement of Rep. McDermott) ("[E]very day millions of Americans gamble on the Internet. Prohibition hasn't prevented the millions of Americans who want to gamble online from doing it. It has forced internet gambling operators to work offshore, it has put consumers at risk, and it sends billions in dollars of revenue to other nations.").

[32] *H.R. 2267, Internet Gambling Regulation, Consumer Protection, and Enforcement Act: Hearing Before the House* (continued...)

Internet Gambling Regulation, Consumer Protection, and Enforcement Act

The Internet Gambling Regulation, Consumer Protection, and Enforcement Act (H.R. 2267) is a bill introduced by the Chairman of the House Financial Services Committee, Representative Barney Frank. The House Financial Services Committee marked up and approved the bill on July 29, 2010. H.R. 2267 would establish a licensing regime under which Internet gambling operators may lawfully accept bets or wagers from individuals located in the United States. Under the bill as originally introduced, the Secretary of the Treasury would have full regulatory authority over the Internet gambling licensing program, including the power to approve, deny, renew, or revoke licenses to operate an Internet gambling facility. However, an amendment adopted by the House Financial Services Committee would permit the Secretary of the Treasury to delegate authority to "qualified State and tribal regulatory bodies" for the purposes of regulating the operation of Internet gambling facilities by licensees and determining the suitability of applicants to obtain a license. Qualified state or tribal authorities would also be allowed to enforce any requirement of the act that is within their jurisdiction.[34]

In addition, H.R. 2267 would establish specific standards and requirements for Internet gambling licensees to satisfy, including the following:[35]

1. Establishing safeguards to verify that the customer placing a bet or wager is of legal age as defined by the law of the state or tribal area in which the individual is located at the time the bet or wager is placed.
2. Requiring mechanisms that verify that the customer placing a bet or wager is physically located in a jurisdiction that permits Internet gambling.
3. Ensuring the collection of all taxes relating to Internet gambling from customers and from any licensee.
4. Maintaining safeguards to combat fraud, money laundering, and the financing of terrorism.
5. Maintaining safeguards to protect the customer's privacy and security.
6. Establishing safeguards to combat compulsive Internet gambling.
7. Maintaining facilities within the United States for processing of bets or wagers made or placed from the United States.[36]

(...continued)

Comm. on Financial Services, 111th Cong., 2nd sess. (2010) (statement of Rep. Paul) ("The ban on Internet gambling infringes upon two freedoms that are important to many Americans: the ability to do with their money as they see fit, and the freedom from government interference with the Internet.").

[33] *Tax Proposals Related to Legislation to Legalize Internet Gambling: Hearing Before the House Comm. on Ways and Means,* 111th Cong., 2nd sess. (2010) (statement of Rep. Frank) ("[B]illions of dollars in taxes … remain uncollected. Enacting these bills would bring this industry out of the shadows, benefit consumers and ensure that all of the revenue does not continue to exclusively benefit offshore operators.").

[34] *See* amendment offered by Rep. Campbell, *available at* http://www.cq.com//displayamendment.do?docid=3712612&productId=1.

[35] H.R. 2267, § 2, adding new 31 U.S.C. § 5383(g).

[36] This requirement was added to H.R. 2267 by an amendment adopted by the House Financial Services Committee. *See* amendment offered by Rep. Campbell, *available at* http://www.cq.com//displayamendment.do?docid=3712612& (continued...)

8. Certifying that they have not committed an intentional felony in violation federal or state gambling laws.[37]
9. Verifying that their customers are not delinquent on their child support.[38]

Indian tribes and states may opt out of the Internet gambling regime if they provide notice to the Secretary of the Treasury; Indian tribes must give notice within 90 days after enactment of the Internet Gambling Regulation, Consumer Protection, and Enforcement Act,[39] while each state has a longer period of time to decide whether to opt-out—a period starting from the enactment of H.R. 2267 and ending on the date on which the state's legislation has conducted one full general legislative session.[40] Therefore, customers located within Indian tribes and states that elected to opt out would be prohibited from engaging in Internet gambling activities,[41] and licensees would be responsible for blocking access to those customers.

An amendment adopted by the House Financial Services Committee would require the Director of the Financial Crimes Enforcement Network, within 120 days after the bill's enactment, to submit to the Treasury Secretary a list of "unlawful Internet gambling enterprises" that identifies any person who has violated UIGEA more than 10 days after the date of the bill's enactment; such a list is to be posted on the Department of the Treasury website for public access and also distributed to "all persons who are required to comply with" the regulations promulgated by the Federal Reserve and the Treasury Department.[42] Another adopted amendment would provide safe harbor from liability for financial institutions that process transactions for licensees, unless they had knowledge that the specific financial activities or transactions are conducted in violation of federal or state laws.[43] Licensees would be prohibited from accepting credit cards as a form of payment with respect to Internet gambling.[44]

Another adopted amendment would prohibit an applicant from obtaining an Internet gambling operating license if the applicant had accepted a bet or wager, paid out winnings or was owned,

(...continued)

productId=1.

[37] This requirement was added to H.R. 2267 by an amendment adopted by the House Financial Services Committee. *See* amendment offered by Rep. Sherman, *available at* http://www.cq.com//displayamendment.do?docid=3712607& productId=1.

[38] This requirement was added to H.R. 2267 by an amendment adopted by the House Financial Services Committee. *See* amendment offered by Rep. Bachmann, *available at* http://www.cq.com//displayamendment.do?docid=3712616& productId=1.

[39] H.R. 2267, adding new 31 U.S.C. § 5386.

[40] Under the bill as originally introduced, states would also be subject to the 90 day time period; however, the House Financial Services Committee adopted an amendment that changed this deadline. *See* amendment text offered by Rep. Brad Sherman, *available at* http://www.cq.com//displayamendment.do?docid=3713770&productId=1.

[41] A state or tribe's decision to opt out does not necessarily mean that persons located within the state or tribal land are prohibited from all Internet gambling activities; rather, the state's governor or the tribal chief must clearly identify the "nature and extent" of the limitation on bets and wagers. H.R. 2267, adding new 31 U.S.C. § 5386.

[42] *See* amendment offered by Rep. Campbell, *available at* http://www.cq.com//displayamendment.do?docid=3712612& productId=1.

[43] *See* manager's amendment offered by Rep. Frank, *available at* http://www.cq.com//displayamendment.do?docid= 3712603&productId=1.

[44] *Id.*

operated, managed or employed by any person who accepted a bet or wager or paid out winnings to an individual, *after* the enactment of UIGEA in 2006, in violation of federal or state law.[45]

The bill (as amended by the House Financial Services Committee) expressly states that no licensee may accept bets or wagers on sporting events, with the exception of pari-mutuel racing as permitted by law (such as horse racing and greyhound racing).[46] In addition, the amended bill would exempt from the new regulatory regime Internet gambling conducted by any state or tribal lottery authority.[47]

Internet Gambling Regulation and Tax Enforcement Act of 2010

Representative McDermott introduced a companion bill to Representative Frank's licensing legislation, the Internet Gambling Regulation and Tax Enforcement Act of 2010 (H.R. 4976). This bill would establish a licensing fee regime within the Internal Revenue Code for Internet gambling operators; it essentially creates a tax on online gambling deposits. H.R. 4976 would require each licensee to pay a monthly Internet gambling license fee in an amount equal to 2% of all funds deposited by customers during that month.[48] According to Representative McDermott, this fee "would never be imposed on a land-based casino. It would level the playing field between online operators and brick-and-mortar gambling operations which are more expensive to run."[49] In addition, the bill provides revenue incentives for states and Native American tribes, as states and tribal authorities have the option of accepting from licensees, on a monthly basis, an online gambling fee "equal to 6 percent of all deposited funds deposited by customers residing in each State or area subject to the jurisdiction of an Indian tribal government."[50] Acceptance of this fee by the state or tribal government relieves the licensee from any obligation to pay any other fee or tax to the state or tribal government relating to online gambling services.

Finally, customers would be required to pay income taxes on their Internet gambling winnings.[51]

In support of the legislation, Representative McDermott noted that the Joint Committee on Taxation estimated that the licensing and regulation of online gambling would generate $42 billion for the federal government over 10 years.[52]

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[45] *See* amendment offered by Rep. Bachus, *available at* http://www.cq.com//displayamendment.do?docid=3712610&productId=1.

[46] *See* amendment offered by Rep. King, available at http://www.cq.com//displayamendment.do?docid=3712608&productId=1.

[47] *See* amendment offered by Rep. Peters, *available at* http://www.cq.com//displayamendment.do?docid=3712617&productId=1. This amendment also provides clarification that the Wire Act (18 U.S.C. § 1084) shall not apply to certain specified activities in connection with Internet gambling conducted by any state or tribal lottery authority. *Id.*

[48] H.R. 4476, § 2(a), adding new 26 U.S.C. § 4491(a).

[49] *Tax Proposals Related to Legislation to Legalize Internet Gambling: Hearing Before the House Comm. on Ways and Means,* 111th Cong., 2nd sess. (2010) (statement of Rep. McDermott).

[50] H.R. 4476, §2(a), adding new 26 U.S.C. § 4493.

[51] H.R. 4476, §6, amending 26 U.S.C. §4401(a).

[52] *Tax Proposals Related to Legislation to Legalize Internet Gambling: Hearing Before the House Comm. on Ways and Means,* 111th Cong., 2nd sess. (2010) (statement of Rep. McDermott), citing Joint Committee on Taxation revenue estimates, *available at* http://www.safeandsecureig.org/media/InternetGamblingScore.pdf. Some have criticized the assumption upon which the $42 billion figure is based, noting that in order to generate $42 billion in new federal revenue, every state and every Native American tribe must be participating in the Internet gambling regime, rather than opting-out. *See H.R. 2267, Internet Gambling Regulation, Consumer Protection, and Enforcement Act: Hearing Before* (continued...)

Internet Poker and Game of Skill Regulation, Consumer Protection, and Enforcement Act of 2009

Senator Menendez introduced the Internet Poker and Game of Skill Regulation, Consumer Protection, and Enforcement Act of 2009 (S. 1597), which offers many of the same provisions as Representative Frank's licensing bill, but only allows the licensing of businesses that operate online games "in which success is predominantly determined by the skill of the players, including poker, chess, bridge, mah-jong, and backgammon";[53] the bill would not permit online betting or wagering with respect to games of chance. Similar to Representative Frank's bill, S. 1597 would allow states and tribes to opt out of the licensing regime. The Director of the Financial Crimes Enforcement Network would be required to submit to the Treasury Secretary a list of "unlawful Internet gambling enterprises" that identifies any person who has violated UIGEA more than 10 days after the date of the bill's enactment.[54] Finally, S. 1597 would impose an Internet gaming license fee similar to Representative McDermott's bill, but instead of 2%, Senator Menendez's bill would require a licensee to pay a monthly federal license fee equal to 5% of its Internet gaming deposited funds for the calendar month.[55] S. 1597 would also require a licensee to also pay a monthly state or tribal government gaming license fee of 5% of the gaming operator's monthly deposits (compared to the 6% that is provided under Representative McDermott's bill).[56] The state or tribal government gaming license fees received in the Treasury of the United States are to be appropriated to a new "State and Indian Tribal Government Gaming License Fee Trust Fund" that the bill would establish.[57] Out of this trust fund, the Treasury Secretary would be required to pay to each qualified state or tribal government an amount of the fees that are attributable to deposits made by persons located within the state or tribal government's jurisdiction.[58]

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the House Comm. on Financial Services, 111th Cong., 2nd sess. (2010) (statement of Tom Malkasian, Vice Chairman, Commerce Casino).

[53] S. 1597, § 102(a), adding new 31 U.S.C. § 5381(5).

[54] *Id.*, § 103(a), adding new 31 U.S.C. § 5368.

[55] *Id.*, § 202(a), adding new 26 U.S.C. § 4491(b)(1).

[56] *Id.*, § 202(a), adding new 26 U.S.C. § 4491(b)(2).

[57] *Id.,* § 202(a), adding new 26 U.S.C. § 9511(a).

[58] *Id.*, § 202(a), adding new 26 U.S.C. § 9511(c).