

## **Summary of Remarks for National Council of Legislators from Gaming States, June 4, 2005 Interactive Gambling (\$7 billion industry and growing)**

Presently, the Internet gambling market is estimated to be between \$7 billion to \$12 billion per year with 76 jurisdictions allowing some form of remote gambling with over 17,000 websites.<sup>1</sup> Most countries that have legalized and regulated interactive gambling will allow licensees to accept wagers from U.S. customers (at least 50 percent of market), e.g., United Kingdom, Malta, Antigua, Isle of Man, Alderney. The United Kingdom attitude is that gambling takes place in the location of the server/licensing country. The U.S. differs (Jay Cohen). Some jurisdictions allowing Internet gambling are underregulated (Curacao) or unregulated (Costa Rica). There are, of course, no restrictions on accepting wagers from U.S. players. Many of the major operators have abandoned online gaming ventures, e.g., Sun International, Harrahs, Tattersalls (only concentrates on lotteries), MGM, because of an inability to access legally the U.S. market.

### **Europe**

Countries having some form of gambling have occasionally taken action against cross-border gambling operators. Within the European Union, members such as Denmark, Italy, Germany, and the Netherlands, have challenged operators from European Union jurisdictions outside their country. In a major decision, *Matter of Gambelli*, the European Court of Justice ruled that a member state may not restrict licensed remote betting services in another European Union jurisdiction without good reason. Preservation of a monopoly or raising revenue are not permissible reasons. Member states have interpreted *Gambelli* differently.<sup>2</sup>

### **International Federation of Horseracing Authorities**

Other jurisdictions opposed to cross-border remote gambling have adhered to the agreement colloquially known as the good neighbor policy. The “semigovernmental” Japanese Racing Association (JRA) persuaded the Japanese government to sign an agreement with Hong Kong whereby neither country would allow its horseracing operators to accept bets from the other country. Other countries have also adopted this “good neighbor policy.” The International Federation of Horseracing Authorities has encouraged other countries to join and by late 2004, approximately 16 other jurisdictions had joined.<sup>3</sup>

What little pressure from the Japanese government against illegal gambling has come from the Japanese Racing Association. One of its officials “said his jaw dropped when he saw a direct mail from Hong Kong, offering odds on all JRA-organized races that were 10 percent better than theirs. The group, based in Canada, was offering its wagers over the phone and online, requiring punters to register a credit card and to open a new bank account for potential winnings. JRA calculates that it is losing up to 14 billion yen annually to these cyber bookies.” The JRA said it hopes to “tackle the freeloaders by all means possible.”<sup>4</sup> The JRA action has so far consisted of asking the policy “to check on such ‘betting’” and asking credit card companies to “freeze settlements involving use of such Internet sites.”<sup>5</sup>

## **United States**

It is the United States that has traditionally been the most antagonistic toward offshore interactive wagering. Since 1995, Congressional bills have been introduced in every session but failed primarily because of the “poison pill”--exemptions for interstate, interactive horseracing and Internet, interstate lotteries. Any bill that does not exempt both does not reach a House or Senate vote and the exemptions may prevent a vote, e.g., Senate 108<sup>th</sup> Congress. The most recent Kyl Bill (Unlawful Internet Gambling Enforcement Act of 2005), expected to be introduced this summer, contains no exemptions.

There is an attempt, the Conyers/Cannon Bill (108<sup>th</sup> Congress) to consider regulations and taxation of interactive gaming. The U.S. Justice Department rarely prosecutes offshore entities and has restricted its activity to pressure financial intermediaries and advertisers, e.g., Esquire.<sup>6</sup>

Among the states, there has been little recent anti-Internet gambling activity. The National Association of [State] Attorneys General have supported Federal legislation. About seven states (most recently Indiana) have passed specific legislation prohibiting some aspect of Internet gambling, but no action has been taken. Some attorneys general (N.Y., N.J.) have taken action against interactive operators or credit card providers.

Two U.S. Jurisdiction, Nevada and the Virgin Islands, have passed legislation or regulations legalizing Internet gambling, but nothing has been done largely because the U.S. Justice Department says interstate, interactive gambling is illegal. The Virgin Islands attorney general disagrees with the Justice Department. North Dakota almost legalized Internet, interstate poker, but the bill failed primarily because the U.S. Justice Department said that the bill would be in violation of federal law.

## **World Trade Organization (WTO)**

Some states, e.g. California, have licensed interstate, interactive horse racing pursuant to a December 2000 amendment to the Interstate Horse Racing Act.<sup>7</sup> The Justice Department said that interstate, Internet horse racing is illegal. Controversy exists concerning Youbet, which in May 2005 received a license for interactive horse racing in Washington state, notwithstanding the state’s conclusion that Youbet had taken bets illegally from State of Washington residents.<sup>8</sup> It was the state-approved interactive horse race wagering that was to be one of the most important issues in the dispute between Antigua and the U.S. before the WTO.

In June 2003, Antigua filed a complaint before the WTO alleging that U.S. policies preventing credit card companies and banks from honoring Antigua online gaming transactions were a violation of the General Agreement on Trade in Services (GATS). It was the first WTO dispute concerning electronic commerce, only the fourth concerning trade in services, and the first dispute to discuss whether public order/public policy would be a valid defense to a restrictive practice.<sup>9</sup> In November 2004, a three-person panel of the WTO concluded that the U.S. was in violation of GATS and that the U.S. should have consulted with Antigua concerning its fears that Antigua licensing offshore gambling violated public policy/public order in that it was harmful to health and susceptible to fraud, underage gambling, and suspicious transactions.<sup>10</sup> On April 7, 2005, the Appellate Body of the WTO ruled that there was no necessity for consultation with Antigua.<sup>11</sup>

The Appellate Board did affirm the Panel finding that the Interstate Horseracing Act might exempt “only *domestic* suppliers of remote betting services for horseracing” from the three federal laws and that the U.S. “has not demonstrated that—in the light of the existence of the IHA—the Wire Act, the Travel Act, and the IGBA (Anti-Gambling Business Act) are applied consistently” with GATS requirements.<sup>12</sup> It would seem that the U.S. might have two choices: amend the Wire Act so as to include foreign horserace access or ban all interactive interstate horseracing.

The immediate reaction of the U.S. loss on many arguments was fear and anger. Senator Orrin Hatch, a widely respected Utah conservative, was upset “especially in light of a recent ruling that said the U.S. and states like Utah may not outlaw Internet gambling. If the WTO system is to work in benefiting all involved, we can’t be forced to bow to the wishes of some obscure island nation and allow our citizens to gamble over the Internet.... It is difficult enough to keep kids away from the lure of easy money. We simply cannot allow other countries to circumvent U.S. and Utah state gambling laws.”<sup>13</sup>

A Utah newspaper also expressed dismay at the ruling. One headline stated, “Get Utah out of WTO.” Another story stated: “The World Trade Organization ruled Thursday that the United States cannot block other countries from offering Internet gambling to U.S. residents, even if they live in states like Utah and Hawaii where gambling is illegal. And under terms of an international trade agreement, Utah could now find itself legally defenseless to stop Internet gaming within its borders. “This WTO ruling opens a box of Pandoras, but it is not surprising given the scope of the WTO’s invasion into domestic spheres of policy making,” said Lori Wallach, director of Public Citizens Global Trade Watch.”<sup>14</sup>

State representatives were unhappy with the lack of federal government consultation with state representatives in the WTO matter.

The Appellate Body basically said the state laws are not in violation, because Antigua didn’t make a good enough case,” a state source said. “It’s just a matter of waiting for the next plaintiff with a better and stronger case.” .... Another state source pointed to the case as a “good example” of where there were not sufficient consultations between the federal government and the affected state interests. He charged that state jurisdiction was negotiated away in an international trade agreement.<sup>15</sup>

One thing is fairly certain. If the U.S. does permit interstate, interactive state lotteries in Georgia, Illinois, or some other state, then it would open the door to renewed WTO litigation.<sup>16</sup>

## **Internet Regulation**

Presently there are two associations, the Interactive Gaming Council and e-COGRA, that attempt to self-regulate interactive gaming.<sup>17</sup> Given the lack of government oversight in the online gaming industry, self-regulations an important part of the debate. Since 1996 the Interactive Gaming Council (IGC) ([www.igcouncil.org](http://www.igcouncil.org)) has continued its advocacy for government regulation. In 2003 a new organization was formed called e-COGRA ([www.ecogra.org](http://www.ecogra.org)) which stands for e-Commerce and Online Gaming Regulation and Assistance. E-COGRA provides seals of approval for sites that meet its standards for fair and responsible online gaming. There have been attempts such as that of the Swiss Institute of Comparative Law to encourage regulators to adopt international standards and rules for Internet gambling. One major problem is that certain jurisdictions, such as Denmark, the Netherlands, the U.S., and Hong Kong, want to prohibit cross-border Internet gambling for different reasons.

## **United Kingdom**

The United Kingdom also licenses betting facilities which are located in Great Britain, and they may accept wagers from the U.S. The United Kingdom has never objected to its land-based casinos setting up offshore operations and taking wagers from citizens of the United States. Its Gambling Bill, enacted into law in April 2005, completely overhauls existing gambling and betting laws and provides for the legalization of remote gambling.

Only about 5 of the 337 sections in the Gambling Bill pertain directly to “remote” or “virtual” gambling. Section 63, Remote Gambling, states a remote operating license is necessary for remote gambling. Section 164 states a virtual gaming license is either for a casino or betting premise. Section 84 states rules for remote licenses that might be established by the soon to be formed Gambling Commission. The major criticism of the British remote gambling legislation is that taxes might be so high they would discourage operators from obtaining a U.K. license.<sup>18</sup>

Great Britain’s gaming legislation is complex and differentiates between casino gambling, lotteries, and various types of betting. While qualifying for casino gambling and lottery operations requires conforming to complex regulations and statutes, a provider of e-betting services needs only to obtain a bookkeepers permit which “is issued by the courts in a fairly straightforward judicial process.” Pool betting also requires regulation as a pool promoter, which necessitates a different procedure which is “again relatively straightforward.”<sup>19</sup> Taxation presently is 15 percent of gross profit on interactive bookmakers and 15 percent tax on betting exchanges.

While gambling and betting laws should undergo a drastic overhaul and revision by the end of 2005, it is fairly apparent that:

- 1) In the meantime, the government has indicated that it will no longer prohibit online gaming advertisements within the U.K.
- 2) The licensed online entities will not be prohibited from accepting wagers from the U.S. and other jurisdictions that have extensive legal gambling.
- 3) Online operators would have to prove suitability and solvency and be incorporated within the U.K. or have a subsidiary company within the U.K.

- 4) Online operators must have policies for the exclusion of underage bettors as well as policies for self-exclusion and maximum stakes.
- 5) Online casinos would be more closely regulated than online betting operations.

### **Compulsive Gambling**

Compulsive gambling<sup>20</sup> litigation has become increasingly common in those jurisdictions that have extensive legalized gambling. There are cases pending in France and Australia. In Austria, a compulsive gambler has been successful in litigation against Casinos Austria.<sup>21</sup> Canadian provinces seem to have the most significant litigation concerning compulsive gambling. In May 2005, a plaintiff who was a compulsive gambler, filed a class action suit against Boeringer and Pfizer claiming defendant claimed to warn “about risks associated with the drug, such as obsessive-compulsive behavior, including compulsive gambling.... The lawsuit is seeking \$3 million on behalf of each claimant, special damages to cover their gambling losses and \$50 million in punitive damages against eh defendants.”<sup>22</sup> A Canadian embezzler may also be more likely to escape incarceration if he alleges the defense of compulsive gambling.

Boyd Dulmage of Ontario, for example, embezzled \$91,000 to support his gambling habit. The judge ordered him to repay the money, perform community service, and remain on probation. There was no jail time since the Ontario Justice concluded: “the Canadian public benefits from gambling on a large scale now,” said Ontario Court Justice Paul Belanger, who noted that more gambling addictions are the inevitable consequence. “The federal, provincial and, to some extent, municipal governments must share some of the responsibility for creating people who fall prey to this addiction.... The responsibility for creating the proverbial monster should be shared.” The Crown attorney had requested 12 to 18 months incarceration.<sup>23</sup>

Presently, there are three major pending cases<sup>24</sup> by Canadian compulsive gamblers in three provinces: Ontario, Quebec, and Nova Scotia. The Ontario lawsuit was filed by Constantin Digalakis and his wife on May 25, 2001, against the OLG, the Falls Management Company, and other gaming defendants for several million dollars each. Digalakis alleged that he was allowed to return to gaming facilities even though he requested self-exclusion. His complaint requested damages of \$1 million based on negligence, breach of contract, and breach of fiduciary duty against certain defendants. The defendants responded and, for example, Windsor Casino Ltd. raised affirmative defenses such as: no duty of care, no fiduciary duty, no loss, release of all claims, voluntary assumption of risk, contributory negligence, and no basis for award of punitive damages. The matter is now in discovery and settlement is a viable possibility.<sup>25</sup>

Unlike Ontario, which does not have Video Lottery Terminals (VLTs), VLTs are the significant factor in two lawsuits that seek class action status in Nova Scotia and Quebec. Bernard Walsh is suing the Nova Scotia government (Nova Scotia Gaming Corp. and the Nova Scotia Alcohol and Gaming Authority) and the Atlantic Lottery Corp. His lawyer, Dick Murtha, has requested class action status on behalf of all gambling addicts in Nova Scotia. He is seeking general damages, special damages, costs of future care and punitive damages, but claims “his main goal is to get the machines out of the province.” In his lawsuit filed September 21, 2004, his statement of claim alleges the defendants introduced and regulated VLT gaming “in a negligent manner” and breached its fiduciary duty to residents of Nova Scotia and “ought to have known of the potential dangers and damages to individuals.”<sup>26</sup>

The most significant lawsuit is the class action litigation in Quebec initiated on May 18, 2001, by Jean Brochu against Loto-Quebec. Brochu, a lawyer, had embezzled \$50,000 from his employer and he blamed the VLTs for his addiction. Unlike other litigants, Brochu received about \$150,000 “in provincial court funding.” On May 6, 2002, the Quebec Court authorized a \$700 million class action (money damages of \$578 million and \$119 million exemplary). The suit may include “any person who, since June 1993, became a compulsive gambler by using video lottery terminals that were put at their disposal and kept in clubs, bars and other public sites by Loto-Quebec.”<sup>27</sup> More than 460 individuals have indicated an interest in joining the class which could rise to approximately 25,000 to 50,000 of the province’s estimated 125,000 compulsive gamblers. The plaintiffs basically allege Loto-Quebec knew or should have known that the VLTs it managed were dangerous because they created a pathological dependency.<sup>28</sup>

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<sup>1</sup> The author is indebted to Michael Tew for this observation. His work “E-Gaming: A Giant Beyond Our Borders” (Bear Stearns, 2002) is cited throughout the WTO Report; see also “Fair, Honest and Safe: Cross-Border Remote Gambling within the European Union,” Association of Remote Gambling Operators Ltd., March 2005 at 14.

<sup>2</sup> Ewout Keuleers, “The Need for a European Framework for Remote Gaming,” (9)(2) *Gaming Law Rev.* (2005) at 134-135.

<sup>3</sup> “Global Deal to Battle ‘Piracy,’” *South China Morning Post*, Oct. 7, 2004.

<sup>4</sup> “JRA Losing Business to Net Raiders,” *Asahi Shimbun*, Dec. 18, 2002.

<sup>5</sup> “JRA to Tighten Control on Illegal Horserace Websites,” *Japan Economic Newswire*, April 14, 2003.

<sup>6</sup> “Esquire Loses Bet vs. Feds—Publisher O’Malley’s Troubles: Millions in Ad Revenue,” *New York Post*, April 20, 2005.

<sup>7</sup> It was this amendment that convinced Gov. Gray Davis to change his mind about interactive wagering; see Jeffrey A. Modisett, “The States and Gaming: A Brief Look at the Past, Present, and Future Through the Eyes of a Former Attorney General,” (6)(2) *Gaming Law Rev.* (2002) at 204.

<sup>8</sup> “Washington Approves Yobet.com,” *IGN*, May 16, 2005.

<sup>9</sup> “United States—Measures Affecting the Cross-Border Supply of Gambling and Betting Services,” *Report of the WTO Panel*, WT/DS285R, Nov. 10, 2004, at par. 6.206, 6.447.

<sup>10</sup> The decision consisting of 287 pages plus annexes/appendices was issued on March 24, 2004, but it was not made public until November 10, 2004, partly in hopes that Antigua and the U.S. would be able to compromise their dispute.

<sup>11</sup> “United States—Measures Affecting the Cross-Border Supply of Gambling and Betting Services,” *Report of the Appellate Body*, April 7, 2005.

<sup>12</sup> *Id.* at par 365, 369. Curiously, the most recent Kyl Anti-Internet Gambling Bill, expected to be introduced this summer, contains no exemption for the interactive interstate horseracing or includes state lotteries.

<sup>13</sup> “Hatch: Utah Must Be Allowed to Ban Net Gambling,” *State News Service*, April 13, 2005.

<sup>14</sup> *Deseret Morning News* (Utah), May 6, 2005, and April 8, 2005.

<sup>15</sup> “Inside U.S. Trade,” [www.insidetrade.com](http://www.insidetrade.com), April 29, 2005.

<sup>16</sup> International Federation of Horseracing Authorities and the World Lottery Association supported the U.S. position on the WTO dispute with Antigua. “Horseracing Supports U.S. Appeal Against WTO Gambling Ruling,” *Press Release*, January 7, 2005; “WLA Supports U.S. in WTO I-gaming Dispute,” *IGN*, Dec. 9, 2003.

<sup>17</sup> Keith Furlong, “Gaming Continues as an Internet Success Story, Despite Obstructions from the U.S. Government: The Industry Uses Self-Regulation to Fill the Void Left by Governmental Inaction,” (9)(3) *Gaming Law Rev.* (2005) at 201-204.

<sup>18</sup> “ARGO Releases Two Reports on Issues Facing Industry,” *IGN*.

<sup>19</sup> Tony Coles, “The United Kingdom,” *Internet Gambling Report*, VII at 396 (2004).

<sup>20</sup> Much of the material on Canada is taken from Alex Igelman and Joseph Kelly, “Status of Canadian Compulsive Gambling Litigation,” (9)(2) *Gaming Law Rev.*, 116-121.

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<sup>21</sup> “French Casino Hit by Lawsuit,” *Crossing Continents*, *BBC News*, Aug. 5, 2004. The gambler alleged the casino breached its duty of care to him.; “Pokie Addicts to Sue for Loss; Rate of Return Illegal—Group,” *Herald Sun* (Melbourne), Dec. 9, 2004; “Gambling Addict Wins a Fortune in Court Ruling Against Casino; Compulsive Player is Compensated by Austrian Operator that Failed to Help Him Kick the Habit,” *Sunday Telegraph* (London), Feb. 22, 2004.

<sup>22</sup> “Suit Blames Parkinson’s Drug for Gambling,” *UPI*, May 10, 2005.

<sup>23</sup> “Confessions of a Gambler: Boyd Dulmage’s betting ‘habit’ cost him everything he had—and then some,” *Ottawa Citizen*, Feb. 22, 2004.

<sup>24</sup> Two Ontario cases by compulsive gamblers, *Dickert v. Ontario Lottery and Gaming Corp., et. al., and Macaluso v. Ontario Lottery and Gaming Corp., et. al.*, were settled out of court; “Gambling Addict, Crown Agency Settle Suit,” *Toronto Star*, Nov. 22, 2003; “HECFI Settles Macaluso Suit for at least \$350,000,” *Hamilton Spectator*, Aug. 14, 2004.

<sup>25</sup> 01-CV-211503; Statement of Defense, Falls Management Company.

<sup>26</sup> “Suit Aims to Kill VLTs; Anti-gambling Crusader Says N.S. Must Pay for Ruined Lives,” *Halifax Herald Ltd.*, Sept. 22, 2004; Case S.H. 199763, Supreme Court of Nova Scotia.

<sup>27</sup> No. 200-06-000017-015; <http://www.canadianlawyermag.com>, Feb. 2002 at 12; Fonds d’aide aux recours collectifs. Additional funding was allowed for the payment of expert testimony; telephone interview with Roger Garneau, attorney for Brochu, Jan. 20, 2005; Judgment, par. 1; On February 21, 2003, the Quebec Court of Appeal rejected Loto-Quebec’s attempt to contest the \$119 million sought as exemplary damages.

<sup>28</sup> “Video Lottery Suicide,” *Montreal Gazette*, Dec. 10, 2001; “If successful each [plaintiff] could receive compensation ranging from \$5,000 to \$50,000 lawyers estimate.”