

**UNLAWFUL INTERNET GAMBLING FUNDING PROHI-
BITION ACT AND THE INTERNET GAMBLING
LICENSING AND REGULATION COMMISSION ACT**

HEARING
BEFORE THE
SUBCOMMITTEE ON CRIME, TERRORISM,
AND HOMELAND SECURITY
OF THE
COMMITTEE ON THE JUDICIARY
HOUSE OF REPRESENTATIVES

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ON

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UNLAWFUL INTERNET GAMBLING FUNDING PROHIBITION ACT AND THE INTERNET GAMBLING LICENSING AND REGULATION COMMISSION ACT

TUESDAY, APRIL 29, 2003

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON CRIME, TERRORISM,
AND HOMELAND SECURITY
COMMITTEE ON THE JUDICIARY,
Washington, DC.

The Subcommittee met, pursuant to notice, at 2:04 p.m., in Room 2237, Rayburn House Office Building, Hon. Howard Coble [Chairman of the Subcommittee] presiding.

Mr. COBLE. Good afternoon, ladies and gentlemen. The Subcommittee on Crime, Terrorism, and Homeland Security will come to order.

Today we are—at the outset I want to apologize to you all for my raspy voice. I have been plagued with a bad cold, so you all bear with me as we go along here.

Today we address a serious and growing problem for our country: the problem of Internet gambling. It is now estimated that \$4.2 billion is wagered over the Internet each year. This is an increase from \$445 million just 6 years ago. There are currently more than 1,800 Internet gambling sites, and the total dollar amount wagered worldwide is expected to reach \$10 billion in the near future.

The most troubling aspect of Internet gambling is the relative ease of accessibility for our Nation's children. The anonymous nature of the Internet makes it almost impossible to prevent underage gamblers from using their parents' credit cards, or even their own in some cases, to log on to a gambling website. Many Internet sites require nothing more than a name, address, and a credit card number. Those sites that do require a person to disclose his or her age make little or no effort to verify this information.

Another group particularly susceptible to Internet gambling are Americans' problem, or addictive gamblers. The National Council on Problem Gambling estimates that there are currently 11 million Americans directly suffering from gambling problems. High rates of financial debt, unemployment, bankruptcy, divorce, homelessness and suicide are all associated with problem gambling. Various casinos and their video game structure have been labeled "the crack cocaine of gambling".

These facilities are open for the most part 24 hours a day, 7 days a week, all within a person's own home. By making gambling more convenient, it can do nothing but make the problem worse.

In addition to the social problems associated with Internet gambling, these Internet sites also offer organized crime groups a very simple and easy opportunity to launder the proceeds of their criminal activity. Because of the lack of oversight or regulations, and the high degree of anonymity, money laundering through Internet gambling sites is already a major concern to our Nation's law enforcement agencies.

Federal law is currently unclear as to whether or not all types of Internet gambling is illegal. The statute that most directly restricts the use of the Internet to place bets is the Wire Act under section 1084 of title 18 of the U.S. Code. However, because this statute was written prior to the age of the Internet and the use of the wireless communication, there is ambiguity as to what type of bettering is or is not covered. Also, the types of gambling mentioned in the statute may not cover all the different types of gambling available on the Internet.

Today we will examine two bills that attempt to address the problems of Internet gambling in two very different ways. H.R. 21, the "Unlawful Internet Gambling Funding Prohibition Act," introduced by our friend from the Heartland, Congressman Jim Leach of Iowa, seeks to ban Internet gambling by prohibiting the use of financial instruments such as credit cards in any transaction involving illegal Internet gambling.

H.R. 3215, the "Combatting Illegal Gambling Reform and Modernization Act," introduced by Congressman John Conyers of Michigan, the Ranking Member of the full Judiciary Committee, seeks to establish a commission to study the feasibility of regulating Internet gambling rather than banning it.

I look forward to the testimony of the witnesses here today, which will help this Subcommittee decide what is the best approach to take with regard to this very important subject.

Now, prior to recognizing the distinguished gentleman from Virginia, the Ranking Member, I am advised that a Member of our Subcommittee will be celebrating a date of birth tomorrow, and with your permission, sir, I will extend a "happy birthday" greeting to you.

I now recognize the Ranking Member.

Mr. SCOTT. Thank you, Mr. Chairman.

You know, when I was growing up, we would always declare a "birthweek." I didn't know that was going to extend to my congressional tenure. Thank you, Mr. Chairman.

I am pleased to join you in convening this hearing regarding the Federal regulation of gambling over the Internet. I would also like to thank you and your staff for working with the minority on a bipartisan matter to develop the hearing and select witnesses for it.

Mr. Chairman, gambling has traditionally been primarily a State regulatory responsibility. It should continue to be so, in my judgment, although it is appropriate for the Federal Government to have a role to assist States in the total regulatory scheme. The Federal Government undertook such a role in passing the 1961 Wire Communications Act as a way to assist the fight against gam-

bling by organized crime syndicates. The Department of Justice contends that it can prosecute Internet gambling businesses under that law, but clearly, that law was not designed with Internet gambling in mind. So I appreciate the desire of my colleague, the gentleman from Iowa, to update the ability of the Department to address illegal gambling in today's context.

However, I am concerned that his bill, H.R. 21, similar to the bills in the last several Congresses which attempted to regulate gambling, is not likely to be effective in doing so. When we address the real question on Internet gambling, we must acknowledge that the horses are literally already out of the gates. So let's be clear that the bill is not about prohibiting Internet gambling; it is only about regulating Internet gambling, and then only with respect to the United States' Internet gambling market.

Regulating anything on the Internet is problematic, even when desirable. Most law enforcement is jurisdictionally dependent. The Internet has no jurisdiction and, as a result, I suspect that, even if we are successful in closing down business sites in the United States, or in countries that we can get to cooperate because of the Internet and electronic funds transfer, the approach of H.R. 21 will be ultimately ineffective. The gambling website can simply code an Internet gambling transaction as another type of transaction and thereby evade the total enforcement mechanism in the bill, or an e-cash or electronic payment system can relocate in another country and thereby evade the enforcement mechanisms in the bill.

Furthermore, we should not overestimate the cooperation we might get from other countries. Presently, over 50 nations allow some form of gambling on line, and that number is likely to grow. And even if we're successful in getting cooperation from most countries, it would simply be increasing the profit opportunities for uncooperative countries, especially those with which the United States does not have diplomatic relations.

To be effective in prosecuting illegal gambling over the Internet, I think we have to prosecute individuals. This bill does not. If we took the approach in this bill in enforcing drug laws, we would be prosecuting the sellers but not the buyers. Prosecuting individuals in Internet gambling would be more effective than what we're seeing in illegal drug prosecutions, because the technology of the Internet would be in the Government's favor, since the activities of illegal gambling would leave a trail leading directly back to the individual gambler. So, so long as individuals can gamble over the Internet with impunity, a market will be provided for them which the regulatory scheme in this bill will not be able to stop.

Since we are not talking about prohibiting Internet gambling but simply regulating it, I believe there is a more effective regulatory approach than offered by H.R. 21. However, the approaches must be developed taking into account the technology, State policies with respect to gambling, and Internet gambling practices and preferences.

This is the approach offered by H.R. 1223, the bill before us authored by Ranking Member of the full Committee, Mr. Conyers. That bill establishes a commission that would study the issue and make recommendations for a regulatory environment for Internet gambling which would be controlled by individual States. States do

tend to prohibit individuals from gambling, so Internet gambling can be both effective and individualized in each State. Under the regulatory environment the bill provides for, if Nevada opts to allow Internet gambling within its borders, it can. If Utah does not opt to allow Internet gambling within its borders, it can prohibit it, and that would be enforceable by the Federal Government by the States that allow gambling, as well as by the State of Utah.

Under such a regulatory environment, it is much more likely that those who choose to gamble over the Internet will do so through a licensed regulated entity than one operating illegally. First, the consumer in a State where Internet gambling is legal will have confidence that, if they win, they will be paid. And in a licensed regulatory entity, such as MGM Mirage.com, we would not have to worry about the licensing authorities in Las Vegas failing to adopt stringent controls on access to its website. A consumer would have no similar confidence in a fly-by-night offshore casino.com, so a likely result from licensing and regulating Internet gaming activities would be to drive less reputable businesses out of business, particularly those that are offshore.

Another significant result is, if States choose to authorize Internet gambling, it can tax it. At a time when unauthorized Internet gambling is flourishing, and when most States are cash-strapped, those States that already have chosen to authorize regulated gambling could receive much more needed revenues while contributing to the control of the industry and protecting the gambling public.

I believe that we should regulate Internet gambling, but we should do it effectively. We should not allow any single business sector with the sole responsibility for doing the bulk of the work of enforcement, whether it is the banking industry as in this bill, or the Internet service industry as we tried in prior bills. There are ways to regulate Internet gambling effectively, and the commission approach to develop those ways is the best way to come up with them.

Again, Mr. Chairman, I thank you for working with us on these two bills. I look forward to hearing the testimony of the witnesses, and I thank you for your birthday congratulations.

Mr. COBLE. You're indeed welcome. And you still don't know how I came into that knowledge. I rarely have him guessing, but I have him guessing now.

Folks, I believe members of the audience need to know something about our panelists, so I'm going to give brief introductory remarks prior to starting with Mr. Leach.

Our first witness is the sponsor of H.R. 21, Representative James Leach. Congressman Leach has been a Member of Congress for 26 years and represents the 2nd District in Iowa. During his tenure, Congressman Leach has invested a tremendous amount of time and effort on the issue of Internet gambling. The Subcommittee looks forward to his testimony on this complex issue.

Our next witness is Mr. John G. Malcolm. Mr. Malcolm is currently a Deputy Assistant Attorney General in the Criminal Division of the Department of Justice, where his duties include overseeing the Computer Crime and Intellectual Property Section, the Child Exploitation and Obscenity Section, the Domestic Security Section, and the Office of Special Investigations.

He is an honors graduate of Columbia College and the Harvard School of Law. Mr. Malcolm served as a law clerk to Judges on both the United States District Court for the Northern District of Georgia, and the 11th Circuit Court of Appeals.

Our third witness is Mr. Jeffrey Modisett. Mr. Modisett is currently counsel for the law firm of Bryan Cave, LLP, in Los Angeles, CA, and has recently published articles concerning the States' approach to on-line gambling, cyber-law, and e-commerce.

An honors graduate of UCLA, Oxford University, and the Yale University School of Law, Mr. Modisett is also the former Indiana Attorney General. Mr. Modisett is the past president of the Family Advocacy Center, which he founded, and a former director of the National District Attorneys Association.

Our final witness this afternoon is Mr. William Hornbuckle. Mr. Hornbuckle is president and chief operating officer of MGM Mirage Online, and executive vice president of marketing for MGM Mirage. He is a 23 year veteran of the gaming industry and was promoted to his current position in July, 2001.

Mr. Hornbuckle has been serving as president and chief operating officer of the MGM Grand Hotel and Casino in Las Vegas since October, 1998. Prior to that role, he was executive vice president of operations for the resort.

It's good to have all of you with us. We have written statements from each of the witnesses on the panel. I ask unanimous consent to submit them into the record in their entirety.

Gentlemen, as you all have previously been told, we try to adhere to the 5-minute rule here, both as to you all and to ourselves. So when that red light illuminates into your face, you will know that you're skating on thin ice. So if you could wrap it up then.

Mr. Leach, before you start, it's good to have you with us. I am a country bluegrass music aficionado, and Merle Haggard, who was known for years as the "country balladeer", once recorded a song entitled, "The Kentucky Gambler." Has anyone in the audience ever heard of the song? Well, the concluding words in his song were these: "...but a gambler loses much more than he wins." A sad story about a guy who abandoned his family because he was an addictive gambler.

So, having said that, Mr. Leach, it's good to have you and the other people with us. Fire away.

**STATEMENT OF HONORABLE JAMES A. LEACH, A
REPRESENTATIVE IN CONGRESS FROM THE STATE OF IOWA**

Mr. LEACH. Thank you very much, Mr. Chairman, Mr. Scott, distinguished Committee counsel. Thank you for holding his hearing. Your leadership on this issue is deeply appreciated.

As I have testified previously in this Committee, gambling on the Internet is fast becoming one of the critical issues confronting thousands of American families. The financial and economic implications of Internet gambling may not be intuitive to those unfamiliar with the workings of the industry, but the consequences cannot be exaggerated. It is simply not good for the economy at large, as well as each individual gambler, but the economy at large, to have Americans send billions to overseas Internet casinos which have shady or unknown owners.

Casino gambling, while it competes for jobs with other sectors of the economy, such as restaurants and the retail trade, also partly balances job losses elsewhere with some job creation. Internet gambling, on the other hand, may be the only sector of the economy where the case of greater efficiency is not altogether compelling. It reduces jobs in competing parts of the American economy, but creates few in itself and all, to date, are abroad. In other words, this is a “jobs” as well as a moral and regulatory issue.

The very characteristics that make the Internet such a valuable resource are also the reasons why it has such a huge potential to impinge on the stability of American financial institutions, as well as the American family. The easy access, anonymity, and speed of transactions which make such positive contributions to the level of efficiency and cost of financial services, also make routine safeguards impractical and leave the financial services industry open to abuse. Internet gambling increases consumer debt, makes bankruptcy more likely, money laundering an easy endeavor, and identity theft a likely burden.

Gambling, in general, and Internet gambling in particular, provide one of the most accessible platforms for money laundering. Money launderers tend to seek out areas where there is a low risk of detection by law enforcement. Internet gambling is a particularly attractive method to launder money because of the heightened level of anonymity and a virtual lack of governmental regulation. Nearly 80 percent of the \$10 billion in revenue generated by Internet gambling sites is impossible to account for, since most operators are located in the Caribbean and other jurisdictions with loose regulatory structures and limited financial reporting requirements.

Reports from the OECD’s Financial Action Task Force specifically point to Internet gambling as a major loophole in anti-money laundering regimes. The U.S. Treasury’s Financial Crimes Enforcement Network has a special anti-money laundering program designed for the traditional domestic gaming industry. No such strategy exists for illegal gambling sites located in unregulated offshore jurisdictions. Given the hard work of this Committee, and also that of the Financial Services Committee, to quash the money laundering efforts of terrorists and narco traffickers, it would be irresponsible to leave such an enormous institutional loophole unplugged.

Suggestions to legalize and regulate Internet gambling address none of these concerns. No regulatory system can prevent the social and economic ramifications of online gambling. This was the conclusion of the National Gambling Impact Study Commission report issued in 1999. This congressionally mandated report concluded that Internet gambling should be illegal at the Federal level and suggested prohibiting the use of financial instruments for these transactions, thus serving as a model for this legislation.

I stress this point, that we have had a national commission on gambling, that was congressionally mandated——

Mr. SCOTT. Jim, did you say it should be legal on the national basis, or illegal?

Mr. LEACH. No, no. Illegal.

Mr. SCOTT. Illegal?

Mr. LEACH. Illegal. I'm sorry. I'm reading a little too quickly. I apologize.

Mr. SCOTT. No, I'm just listening too slowly.

Mr. LEACH. While it's true that one can have more formalized prohibitions—and I would certainly favor them—it is not necessarily the case that it is easy to get Congress to adopt bigger steps, so this bill is designed to accept the law, whatever this Committee determines to be, and then, using the Banking Committee's jurisdiction, come up with an approach which is basically functional regulation or a functional deterrent to whatever laws this Committee determines are appropriate.

I would simply stress that this is a functional ban. It is partly working today because, voluntarily, several of the major credit card companies have taken this direction as their own practice. We have already seen the Bear Stearns report that about half the Internet gambling profits have been reduced, and a number of companies are seeing some difficulties based on certain voluntary steps in this direction. So an assertion that there is no effectiveness defies the current partial steps that are being taken in the private sector.

In conclusion, let me stress that at a personal level I am a skeptic about all forms of gambling. But each of us are obligated to the maximum extent possible to be respectful of legitimate choices made by others. Casino gambling, as it exists in America, is at least regulated by the State to protect the participants. Generally, casinos also add entertainment and involve elements of socialization.

Gambling alone, on the other hand, whether using a laptop at home or a computer in the workplace, involves no entertainment or socialization element, and lacks the fundamental protections of law and regulation. Casino gambling, as it has been sanctioned in all Western democracies, has only been allowed to exist with comprehensive regulation. Internet gambling lacks such safeguards. It is a danger to the family and society at large. It should be ended.

From a family perspective, the home may be considered a castle, but it should never be a casino.

Thank you all very much.

[The prepared statement of Mr. Leach follows:]

PREPARED STATEMENT OF THE HONORABLE JAMES A. LEACH, A REPRESENTATIVE IN
CONGRESS FROM THE STATE OF IOWA

Mr. Chairman, thank you for holding this hearing on legislation addressing the epidemic problem of Internet gambling. Your leadership on this issue is deeply appreciated.

As I testified previously, gambling on the Internet is fast becoming one of the most critical issues confronting thousands of American families and the social and economic implications of Internet gambling can no longer be ignored. The ramifications of Internet gambling are now showing themselves on college campuses and even professional athletes have admitted addiction. Approximately 15 million Americans are at-risk or problem gamblers, who are more likely to have drug addictions, alcohol dependency, serious family dysfunction, and, at the extreme, especially when gambling losses accumulate, a higher rate of suicide.

The financial and economic implications of Internet gambling may not be intuitive to those unfamiliar with the workings of the industry, but the consequences cannot be exaggerated.

It simply is not good for the economy at large to have Americans send billions to overseas Internet casinos which often have shady or unknown owners.

Casino gambling, while it competes for jobs with other sectors of the economy, such as restaurants and the retail trade, also partly balances job losses elsewhere

with some job creation. Internet gambling, on the other hand, may be the only sector of the economy where the case of greater efficiency is not altogether compelling. It reduces jobs in competing parts of the American economy, but creates few in itself and all, to date, are abroad. In other words, this is a "jobs" as well as a moral and regulatory issue.

The very characteristics that make the Internet such a valuable resource are also the reasons why it has such a huge potential to impinge on the stability of American financial institutions, as well as the American family. The easy access, anonymity, and speed of transactions which make such positive contributions to the level of efficiency and cost of financial services also make routine safeguards impractical and leave the financial services industry open to abuse. Internet gambling increases consumer debt, makes bankruptcy more likely, money laundering an easy endeavor, and identity theft a likely burden.

Gambling in general and Internet gambling in particular provide one of the most accessible platforms for money laundering. Money launderers tend to seek out areas where there is a low risk of detection by law enforcement. Internet gambling is a particularly attractive method to launder money because of the heightened level of anonymity and a virtual lack of governmental regulation. Nearly 80 percent of the \$10 billion in revenue generated by Internet gambling sites is impossible to account for, since most operators are located in the Caribbean and other jurisdiction with loose regulatory structures and limited financial reporting requirements.

Reports from the OECD's Financial Action Task Force specifically point to Internet gambling as a major loophole in anti-money laundering regimes. The U.S. Treasury's Financial Crimes Enforcement Network has a special anti-money laundering program designed for the traditional domestic gaming industry. No such strategy exists for illegal gambling sites located in unregulated offshore jurisdictions. Given the hard work of this Committee, and also that of the Financial Services Committee, to quash the money laundering efforts of terrorists and narco-traffickers, it would be irresponsible to leave such an enormous institutional loop-hole unplugged.

Suggestions to legalize and regulate Internet gambling address none of these concerns. No Internet gambling site will subject themselves to taxation and the cost of regulation when they can remain offshore. And no regulatory system can prevent the social and economic ramifications of online gambling. This was the conclusion of the National Gambling Impact Study Commission Report issued in 1999. This congressionally mandated report concluded that Internet gambling should be illegal at the federal level and suggested prohibiting the use of financial instruments for these transactions, thus serving as a model for this legislation.

In conclusion, let me stress that at a personal level I am a skeptic about all forms of gambling, but each of us are obligated to the maximum extent possible to be respectful of legitimate choices made by others. Casino gambling as it exists in America is, at least, regulated by the State to protect the participants. Generally, casinos also add entertainment and involve elements of socialization. Gambling alone, on the other hand, whether using a laptop at home or a computer in the workplace, involves no entertainment or socialization element and lacks the fundamental protections of law and regulation. Casino gambling as it has been sanctioned in all Western democracies has only been allowed to exist with comprehensive regulation. Internet gambling lacks such safeguards. It is a danger to the family and society at large. It should be ended.

From a family perspective, the home may be considered a castle; but it should never be a casino.

Thank you.

Mr. COBLE. Thank you, Mr. Leach.

We have been joined by the gentleman from Florida, Mr. Feeney, and Mr. Chabot, the gentleman from Ohio.

Mr. Malcolm.

STATEMENT OF JOHN G. MALCOLM, DEPUTY ASSISTANT ATTORNEY GENERAL, CRIMINAL DIVISION, U.S. DEPARTMENT OF JUSTICE

Mr. MALCOLM. Mr. Chairman, Members of the Subcommittee, thank you for inviting me to testify today. The issue before the Subcommittee is one of singular importance and I commend the Subcommittee for holding this hearing.

I would also like to commend Congressman Leach, as well as Congressman Goodlatte and Senator Kyl, for their tireless efforts and longstanding commitment to provide law enforcement with additional tools to combat Internet gambling. Today, I am pleased to offer the views of the Department of Justice about Internet gambling.

As you all know, the number of Internet gambling sites has increased substantially in recent years. While there were approximately 700 Internet gambling sites in 1999, it is estimated that, by the end of 2003, there will be approximately 1,800 such sites, generating between \$4.2 and \$4.3 billion. In addition to online casino-style gambling sites, there are numerous offshore sports book operations that take bets both over the Internet and via the telephone. These developments are of great concern to the United States Department of Justice because of the potential for fraud, the opportunities they create for money launderers and organized criminal organizations, and the problems of gambling by minors and by compulsive gamblers, which are exacerbated by Internet gambling. I discuss each of these issues in greater detail in my written testimony.

Additionally, most of these gambling businesses operate offshore in foreign jurisdictions. Many of them accept bets from United States citizens, which is a violation of several Federal laws, including sections 1084, 1952 and 1955 of title 18, United States Code.

The Department of Justice generally supports the efforts of the drafters of H.R. 21, to enable law enforcement to cut off the transfer of funds to and from illegal Internet gambling businesses.

With respect to H.R. 1223, the Department has concerns about the feasibility and desirability of regulating Internet gambling. I have more extensive comments on H.R. 21 and H.R. 1223 in my written testimony. Of course, I am happy to answer any questions you may have about those bills.

Before concluding, I would just like to thank you again for inviting me to testify today. The Justice Department also thanks you for your support over the years, and we reaffirm our commitment to work with Congress to address the significant issue of Internet gambling.

Thank you.

[The prepared statement of Mr. Malcolm follows:]

PREPARED STATEMENT OF JOHN G. MALCOLM

Mr. Chairman and Members of the Subcommittee:

Thank you for inviting me to testify today. The issue before this Subcommittee is one of singular importance, and I commend the Subcommittee for holding this hearing. I would also like to commend Congressman Leach, as well as Congressman Goodlatte and Senator Kyl, for their tireless efforts and longstanding commitment to provide law enforcement with additional tools to combat Internet gambling. Today I am pleased to offer the views of the Department of Justice about Internet gambling, including the potential for gambling by minors and compulsive gamblers, the potential for fraud and money laundering, the potential for infiltration by organized crime, and recent state actions. The Department of Justice generally supports the efforts of the drafters of H.R. 21 and S. 627 to enable law enforcement to cut off the transfer of funds to and from illegal Internet gambling businesses. With respect to H.R. 1223, the Department has concerns, which I shall address below, about the feasibility and desirability of regulating Internet gambling.

As you all know, the number of Internet gambling sites has increased substantially in recent years. While there were approximately 700 Internet gambling sites

in 1999, it is estimated that by the end of 2003, there will be approximately 1,800 such sites generating around \$4.2 billion. In addition to on-line casino-style gambling sites, there are numerous off-shore sports books operations that take bets both over the Internet and via the telephone. These developments are of great concern to the United States Department of Justice, particularly because many of these operations are currently accepting bets from United States citizens, when it is illegal to do so.

The Internet and other emerging technologies, such as interactive television, have made possible types of gambling that were not feasible a few years ago. For example, a United States citizen can now, from his or her home at any hour of the day or night, participate in an interactive Internet poker game operated by a computer located in the Caribbean. Indeed, a tech-savvy gambler can route his bets through computers located in other countries, thereby obscuring the fact that he is placing his bet from the United States.

GAMBLING BY MINORS

On-line gambling also makes it far more difficult to prevent minors from gambling. Unlike traditional physical casinos and Off-Track-Betting parlors, the operators of gambling websites cannot look at their customers to assess their age and request photo identification. Currently, Internet gambling businesses have no reliable way of confirming that gamblers on their website are not minors who have gained access to a credit card. Although some companies are developing software to try to detect whether a player is old enough to gamble or whether that player is from a legal jurisdiction, such software has not been perfected and would, of course, be subject to the same types of flaws and vulnerabilities that could be exploited by hackers.

COMPULSIVE GAMBLING

Unlike on-site gambling, on-line gambling is readily available to anyone with an Internet connection at all hours of the day or night. This presents a particular danger for compulsive gamblers. As was recently pointed out by the American Psychiatric Society: "Internet gambling, unlike many other forms of gambling activity, is a solitary activity, which makes it even more dangerous; people can gamble uninterrupted and undetected for unlimited periods of time." Indeed, the problems associated with pathological and problem gamblers, a frighteningly-large percentage of which are young people, are well-established and can be measured in the ruined lives of both the gamblers themselves and their families.

POTENTIAL FOR FRAUD

Although there are certainly legitimate companies that either are operating or want to operate on-line casinos in an honest manner, the potential for fraud connected with casinos and bookmaking operations in the virtual world is far greater than in the physical realm. On-line casinos and bookmaking establishments operate in many countries where effective regulation and law enforcement is minimal or non-existent. Start-up costs are relatively low, and cheap servers and unsophisticated software are readily-available. Like scam telemarketing operations, on-line gambling establishments appear and disappear with regularity, collecting from losers and not paying winners, and with little fear of being apprehended and prosecuted.

Through slight alterations of the software, unscrupulous gambling operations can manipulate the odds in their favor, make unauthorized credit card charges to the accounts of unsuspecting gamblers, or alter their own accounts to skim money. There is also a danger that hackers can manipulate the online games in their favor or can steal credit card or other information about other gamblers using the site.

POTENTIAL FOR ORGANIZED CRIME

Additionally, the Department of Justice is concerned about the potential involvement of organized crime in Internet gambling. Traditionally, gambling has been one of the staple activities in which organized crime has been involved, and many indictments brought against organized crime members have included gambling charges. We have now seen evidence that organized crime is moving into Internet gambling.

INTERNET GAMBLING VIOLATES FEDERAL LAW

Most of these gambling businesses operate offshore in foreign jurisdictions. If they are accepting bets or wagers from customers located in the United States, then these businesses are violating federal laws, including Sections 1084, 1952, and 1955

of Title 18, United States Code. While the United States can indict these companies or the individuals operating these companies, it may be difficult to bring them to trial in the United States.

MONEY LAUNDERING AND INTERNET GAMBLING

Another major concern that the Department of Justice has about on-line gambling is that such businesses provide criminals with an easy and excellent vehicle for money laundering. This is due in large part to the cash-intensive nature of the industry, the fact that most Internet gambling sites are located offshore, and the volume, speed, and international reach of Internet transactions.

It is a fact that money launderers have to go to financial institutions to conceal their illegal funds and to recycle those funds back into the economy for their use. Because criminals are well aware of the fact that banks are now subject to greater scrutiny and regulation, they have—not surprisingly—turned to other non-bank financial institutions to launder their money. On-line casinos are a particularly inviting target because, in addition to using the gambling that on-line casinos offer as a way to hide or transfer money, on-line casinos offer a broad array of financial services to their customers, such as providing credit accounts, fund transmittal services, check cashing services, and currency exchange services.

Individuals wanting to launder ill-gotten gains through an on-line casino can do so in a variety of ways. For example, a customer could establish an account with a casino using illegally-derived proceeds, conduct a minimal amount of betting or engage in offsetting bets with an overseas confederate, and then request repayment from the casino, thereby providing a new “source” of the funds. If a gambler wants to transfer money to an inside source in the casino, who may be located in another country, he can just play until he loses the requisite amount. Similarly, if an insider wants to transfer money to the gambler, perhaps as payment for some illicit activity, he can rig the game so the bettor wins.

The anonymous nature of the Internet and the use of encryption make it difficult to trace the transactions. Further, the gambling business may not maintain the transaction records, in which case tracing may be impossible. While regulators in the United States can visit physical casinos, observe their operations, and examine their books and records to ensure compliance with regulations, this is far more difficult, if not impossible, with virtual casinos.

COMMENTS ON H.R. 1223

If enacted, H.R. 1223 would establish a Commission to study the existing legal framework governing Internet gambling and the issues involved with the licensing and regulation of Internet gambling. Among the topics to be studied, the Commission would review existing law, assess the impact of Internet gambling on problem gamblers and minors, assess the susceptibility of Internet gambling to money laundering, and study the potential of regulatory measures to minimize any adverse problems. As I previously stated, the Department has concerns about these and other issues as they relate to Internet gambling. At this time, the Department believes that Internet gambling should be prohibited for many of the reasons I have mentioned, as well as others cited by the Congressionally-created National Gambling Impact Study Commission in its 1999 Report recommending that Internet gambling be prohibited. Moreover, given differences in state law on the issue of gambling in general, and given the fact that Internet gamblers could come from any state, the Department also has concerns that such regulation would need to ensure that the laws of all states were taken into consideration when analyzing this issue.

While the Department would not necessarily oppose *per se* a Commission that would revisit these issues and make recommendations on the feasibility of regulating Internet gambling, H.R. 1223 provides that this Commission **shall** issue proposed changes to Federal law and regulations to provide for the licensing and regulation of Internet gambling in the United States. This requirement appears to pre-ordain the outcome of the Commission’s study and not permit this Commission to reach the same conclusion that the National Gambling Impact Study Commission reached just four years ago, to wit, that Internet gambling be prohibited and not regulated.

Our review of H.R. 1223 is continuing, and we may have additional comments at a later date. But if Congress elects to consider legislation, such as H.R. 1223, that could, in theory, eventually lead to the legalization of Internet gambling, it will be very important to bear in mind and emphasize the debilitating and potentially disastrous consequences of such a step that I noted previously—namely, the problems of underage gambling, addictive gambling, and fraud, as well as the possibility of organized crime involvement.

Even if H.R. 1223 is enacted, that should not preclude action on H.R. 21 and S. 627, since these bills apply only to “unlawful Internet gambling” and would not be applicable to lawful Internet gambling. Given that illegal gambling exists in the physical world despite the availability of legalized forms of gambling in many states, there is every reason to believe that unlawful gambling would continue to exist in the cyber world even if the United States were to regulate Internet gambling.

COMMENTS ON H.R. 21

The Department has several comments on H.R. 21. First, the Justice Department believes that H.R. 21 should apply to all means of wagering that derive from the Internet. Many offshore sports books accept wagers both over the telephone and over the Internet. As drafted, H.R. 21 is only applicable to Internet gambling, so an otherwise illegal site could avoid the bill’s prohibitions by directing that wagers be placed over the phone rather than via the Internet. The bill should apply to all unlawful Internet gambling regardless of the communications medium being used to place bets.

Second, the Justice Department opposes provisions of H.R. 21 that weaken or alter existing federal law or standards. The Justice Department recognizes the important role that federal regulators play in regulating federally-insured financial institutions and is currently discussing with the Treasury Department procedures whereby injunctive relief would only be sought in full coordination with the appropriate federal financial regulator. Nonetheless, the Justice Department believes that Rule 65 of the Federal Rules of Civil Procedure should be the sole standard used by courts in considering whether to grant injunctive relief. Section 3(c)(5)(B) of H.R. 21 sets forth additional factors that the district court must consider in determining whether to grant injunctive relief against certain entities, including credit card issuers and financial institutions. Rule 65 is the well-established standard used in federal courts throughout the country in all cases in which a party is seeking injunctive relief, and the Department opposes any attempt to alter existing federal standards for the benefit of specific entities. Moreover, the Department believes that, under a standard Rule 65 analysis, a district court would already have the discretion to consider the listed factors.

For the same reason, the Justice Department opposes Section 3(c)(4)(B) of H.R. 21, which provides, in essence, that interactive service providers that are not liable under H.R. 21 shall not be liable under Section 1084 of Title 18, United States Code, unless the ISP has actual knowledge of the bets and wagers **and** owns, controls, operates, manages, supervises, or directs a website at which unlawful bets or wagers are offered, placed, or received. This provision constructively amends Section 1084, an existing federal criminal statute, and weakens its application by imposing a far higher standard of liability than traditional aiding and abetting liability, which applies to everyone else who must comply with the law. While the Department does not believe that ISPs should be singled out for particularly harsh treatment (and our “track record” bears this out), we do not believe that ISPs should be singled out for uniquely favorable treatment either.

Third, the Justice Department has other concerns about how the bill treats ISPs, particularly as it pertains to the removal of Internet gambling websites and the cessation of ancillary services connected to those sites. We are, however, working diligently with representatives from several prominent interactive service providers.

CONCLUSION

On behalf of the Department of Justice, I want to thank you again for inviting me to testify today. We thank you for your support over the years and reaffirm our commitment to work with Congress to address the significant issue of Internet gambling. I will be happy to answer any questions that you might have.

Mr. COBLE. Mr. Malcolm, your eyes weren’t even close to being fixated. You finished well ahead of the red light and I commend you for that.

We have been joined by the gentlelady from Texas, Miss Jackson Lee. It’s good to have you with us, Sheila.

Thank you, Mr. Malcolm.

Mr. Modisett, am I pronouncing your surname correctly?

Mr. MODISETT. You are, thank you.

Mr. COBLE. It’s good to have you with us, Mr. Modisett.

STATEMENT OF JEFFREY MODISETT, COUNSEL, BRYAN CAVE, LLP, AND FORMER ATTORNEY GENERAL, STATE OF INDIANA

Mr. MODISETT. Thanks very much.

Mr. Chairman and Members of the Committee, thank you for the opportunity to testify today on this complex issue.

I have come to this issue today with both a law enforcement and technology background. As you noted, I have been a Federal prosecutor, a D.A., a State attorney general, but I have also worked in Silicon Valley and currently represent some high tech clients. The views I express today are my own.

As Indiana Attorney General, I issued an official opinion on Internet gaming. In that opinion, I wrote that, under Indiana law, only gambling that is specifically authorized by statute is legal. Since there are no references to Internet gaming in the Indiana code, it's not legal.

But the question of whether the Federal Government should proactively attempt to prohibit all Internet gaming preemptively is a different question. My experience convinces me that the best antidote to an unregulated, offshore Internet gambling industry is a fully licensed, highly regulated, onshore Internet gambling industry based on strict American standards and priorities. I would further suggest that the enforcement mechanism proposed in H.R. 21, while well intended, is likely to be ineffective, counter-productive, and prone to unintended consequences.

H.R. 21 seeks to have the financial institutions operating in America prevent Americans from using financial instruments to place online wagers. I'm aware that one of the ostensible reasons for this effort is the fear that Internet gambling will provide an avenue for money laundering. Frankly, I find this assertion strange, given that the majority of Internet wagers are placed by credit cards, and credit card transactions are almost always transparent.

I don't believe that H.R. 21 will stop Americans from gambling on the Internet. I do believe it will change the manner in which they do so. If Internet gamblers cannot use their credit cards, many and perhaps most of them will instead opt for e-cash accounts, electronic fund transfers, wire transfers to accounts at offshore banks, and other less visible means to settle their accounts.

It is impossible to predict, but none of the foregoing financial transactions are particularly difficult to execute. The added inconvenience might stop a few people who are rare or occasional bettors, but it won't stop experienced gamblers, including problem gamblers.

What the legislation will do, however, is potentially worsen the very problem it sets out to solve. To the extent that there's a potential for money laundering in the Internet gaming space—and the financial industry itself believes that this potential is small, according to the GAO—creating a market for less transparent payment solutions will presumably make illicit activities, including money laundering, substantially worse. Creating a market for blind e-cash is not the way to stop money laundering. The way to stop it is to make sure Internet gaming takes place in highly regulated, supervisory regimes.

I don't want American financial institutions to act as our police on the Internet. They will err on the side of over-inclusion and pro-

hibit legal transactions out of an overabundance of caution, as they already have. We have not regulated Internet activity so directly before now, and now, at a time when the current law is unsettled, is not the time to begin.

Admittedly, the commission envisioned by H.R. 1223 would have a difficult job, but if it's achieved, the results would solve many of the problems that the prohibitionists sincerely want to solve. In a licensed environment, it is possible to verify identity online, using pin numbers and out-of-session contacts. This and other technology could be used to help ensure no minors gamble on the Internet.

Because all Internet gaming transactions are recorded, it is actually easier to track problem gamblers in the cyber world than in the bricks and mortar casino. Self-exclusion and preset loss limits are more easily accomplished.

Another benefit would be economic. Instead of flowing offshore, the money wagered on the Internet would remain in the U.S. and help build the economies of the regulating States.

Mr. Chairman, when Evan Bayh became Governor of Indiana, he did not support gambling, but the people spoke and voted for a repeal of our constitutional ban on gambling. Governor Bayh concluded that if gambling was to be legal in Indiana, he would appoint people of unquestionable integrity and with law enforcement background to head up the regulatory effort. It worked. The Federal Government should also acknowledge now that Internet gaming will continue to grow in America, and we should appoint tough, fair-minded people with integrity to develop model approaches and help establish international standards for Internet gaming regulation.

In summary, Mr. Chairman, I don't believe the choice before the Subcommittee is whether or not there will be Internet gambling in the U.S. There will be. The question is what sort of Internet gambling there will be. Under H.R. 21, it will be an unlicensed, unregulated industry, where the Federal and State governments afford no protection, and with no economic benefit or tax revenue accruing to the U.S.

Under H.R. 1223, there is the potential for a tightly regulated industry, overseen by Americans of integrity, bolstered by laws and regulations that provide substantial protections for minors and problem gamblers, remove the potential for money laundering, and provide economic benefit and tax revenue in the U.S.

Once again, thank you for the opportunity to testify. I look forward to the questions.

[The prepared statement of Mr. Modisett follows:]

PREPARED STATEMENT OF JEFFREY A. MODISETT

Mr. Chairman and members of the Committee, let me begin by thanking you for the opportunity to testify today on this complex issue.

It is difficult to discuss my opinion on the topics at issue today without putting it in the context of my personal experience and so, with your permission, I would like to briefly mention the more relevant part of my background.

Upon graduation from Yale Law School and following a clerkship with a federal judge, I began my career as an Assistant U.S. Attorney in Los Angeles. In time, I became the Deputy Chief of the Public Corruption and Government Fraud Unit, specializing in the prosecution of violations of the U.S. Export Control laws. In 1988, I returned to my home state of Indiana to work for Evan Bayh (now Senator Bayh), first on his successful gubernatorial campaign and then as his Executive Assistant

for Public Safety. In this capacity, I served as Governor Bayh's liaison to the State Police, Department of Correction, and National Guard, as well as headed up the state's efforts in the war on drugs. In 1990, I was elected Prosecuting Attorney for Marion County, Indiana, which is the City of Indianapolis. In 1996, I was elected state attorney general.

As attorney general, I issued official opinions, including one on Internet gaming. That Official Opinion, by the way, concluded that Internet gaming is illegal in Indiana. At the Governor's request, I also chaired the state's Gambling Impact Study Commission. The Commission met for two years and issued a lengthy report in December 1999.

Today, the committee has before it two bills, H.R. 21 and H.R. 1223, which pursue two very different approaches to Internet gambling. To oversimplify, H.R. 21 seeks to enforce a prohibition on Internet gambling, while H.R. 1223 seeks to create a commission to determine how states and the federal government might work together to license and regulate Internet gaming. Personally, I believe that H.R. 21 has great surface appeal, especially (of course) for those who oppose gambling in all forms. However, it is my opinion that H.R. 1223 is the preferable approach; the reasons for this will be the focus of my testimony.

Internet gambling raises many thorny issues. There are the social, fiscal, and economic impacts of all legalized gambling—which were the focus of our two-year study in Indiana. There is a question of political philosophy, that is, how much should the government do to protect people from themselves, and to what extent the freedoms of the many should be restricted to protect the vulnerabilities of the few. There is the perplexing question of how to apply the varying state and federal laws and regulations to transactions that are trans-jurisdictional by their very nature. Finally, there are more nuanced questions about the differences among sportsbook, casino-style, lottery, pari-mutuel and other forms of gaming, and how the law should treat each of these.

In dealing with all of these things, there are a few points upon which I believe we all agree. I believe we all seek to minimize the adverse consequences that can accompany gambling—we must do all we can to prevent gambling by minors, we must be vigilant to identify pathological gambling and have the tools and resources for dealing with it when we find it, and we must investigate the potential for money laundering. I also think we all agree that most Americans today have the option to gamble if they so choose—only three states prohibit all gambling, and even in those states, illegal gambling is an option. There is no *legal* sports betting outside of Nevada, and yet there is plenty of sports betting across the country. And, I think we can all agree that Americans who want to gamble on the Internet are almost certainly going to be able to do so—they can today, and they will be able to do so in the future. Unless the federal government wants to take draconian steps that would adversely affect both the Internet and personal privacy, people who want to bet on the Internet will be able to do so.

As I mentioned earlier, as Indiana Attorney General, I issued an Official Opinion, which still has precedential authority in Indiana. In that Opinion, I wrote that under Indiana law only gambling that is specifically authorized by statute is legal. Since there are no references to Internet gaming in the Indiana Code, it is not legal—even though gambling on riverboats, on horse races, and by lotteries are explicitly permitted in some fashion. I also warned in that Opinion that many Hoosiers were likely gambling over the Internet anyway, and that therefore parents especially should be mindful of how easy it is to gamble on-line. This Opinion was widely interpreted as calling prospectively for the outright prohibition of gambling on the Internet, which was not accurate. As attorney general, I had an obligation to advise my constituents on Indiana law as it then existed. But my Opinion, as reinforced by my service on the state Gambling Impact Study Commission and other experiences, was and is more complicated and nuanced than the position advanced by the prohibitionists.

I submit that the best antidote to an unregulated offshore Internet gambling industry is a fully-licensed, highly-regulated on-shore Internet gambling industry based on strict American standards and priorities. I would further suggest that the enforcement mechanism proposed in Congressman Leach's bill—while well-intended—is likely to be ineffective, counter-productive, and prone to unintended consequences.

PROBLEMS WITH THE LEACH BILL

H.R. 21 seeks to have the financial institutions operating in America prevent Americans from using financial instruments to place on-line wagers. It would have the Department of the Treasury adopt regulations aimed at blocking such wagers,

and would empower state and local law enforcement to seek injunctions to require financial institutions to take additional enforcement steps.

I am aware that one of the ostensible reasons for this effort is a fear that Internet gambling will provide an avenue for money laundering. Frankly, I find this assertion strange, given that the majority of Internet wagers are placed by credit cards, and credit card transactions are almost always transparent. I do not believe that the Leach bill will stop Americans from gambling on the Internet; however, I do believe it will change the manner in which they do so.

If Internet gamblers cannot use their credit cards, many (perhaps most) of them will instead opt for e-cash accounts, electronic funds transfers, wire transfers to accounts at offshore banks, and other less visible means to settle their accounts. Presumably, the bills' sponsors proceed from the assumption that added inconvenience will dissuade many or most gamblers from betting on-line. It is impossible to predict, but none of the foregoing financial transactions are particularly difficult to execute. The added inconvenience might stop a few people who are rare or only occasional bettors. But it will certainly not stop experienced gamblers, including problem gamblers.

What this legislation will do, however, is potentially worsen the very problem that it sets out to solve. To the extent that there is a potential for money laundering in the Internet gaming space, creating a market for less transparent payment solutions will presumably make illicit activities, including money laundering, substantially worse. The obvious response to the Leach bill by the offshore industry will be to create payment solutions that U.S. law enforcement and U.S. banks cannot easily "see"—that is, their transactions will be harder to trace. Creating a market for blind e-cash is not the way to stop money laundering.

SOLUTIONS IN THE CONYERS BILL

Admittedly, the commission envisioned by H.R. 1223 would have a difficult job. The members would have to determine how best to preserve state prerogatives in an Interstate medium. They would have to provide guidance on which regulations will keep minors and pathological gamblers from betting on-line, at least affording the same level of protections as exist in land-based casinos. They would have to recommend means to protect against money laundering. They would have to ensure the fairness of games and ensure that winnings are paid out. Finally, they would have to figure out how to appropriately tax the proceeds of Internet wagers.

But if this is achieved, the results would solve many of the problems that the prohibitionists sincerely want to solve. In a licensed environment, it is possible to verify identity on-line using PIN numbers and out-of-session contacts. This and other technology could be used to help ensure no minors gamble on the Internet. Because all Internet gaming transactions are recorded, it is actually easier to track problem gamblers in the cyberworld than in a brick-and-mortar casino. Self-exclusion and pre-set loss limits are more easily accomplished.

Another benefit would be economic—instead of flowing offshore, the money wagered on the Internet would remain in the U.S. and help build the economies of the regulating states. One may oppose gambling for various reasons, but it is undeniable that local economies have benefited from gambling and state and local governments have gained revenues from it. States could also collect taxes on Internet gambling that they are losing today (from both casinos and bettors); this would help with the substantial budget shortfalls most states now face. I would not propose Internet gaming as a way of fixing state deficits, but I would suggest that the revenue generated from American bettors in cyberspace should help the United States and not Netherland Antilles or the Grand Cayman Islands.

I should be clear: I most certainly am not an advocate of H.R. 1223 for economic reasons. I think there are better ways for government to improve people's lives economically. But I do think it is short-sighted to think that we can have any significant impact on such a huge industry as Internet gaming by convincing ourselves that we can stop offshore cybergaming at the border. Instead, and most importantly, we should minimize and marginalize the offshore Internet gaming industry by developing a fully-licensed, highly-regulated industry in the U.S. We should use the marketplace to "suck all of the oxygen" out of the offshore industry. U.S. customers prefer U.S. brands and U.S. companies would quickly dominate the market. In terms of the U.S. market, much of the offshore industry would probably give up entirely and shift their focus from the U.S. to other countries where they might have a better chance of competing successfully. In the meantime, U.S. companies would set the standard for fairness and honesty because they would be operating under a fully transparent regulatory regime.

In fact, dozens of countries have already begun the process of licensing and regulating Internet gambling—most notably the United Kingdom. The U.K.'s licensing and regulation regime will be complete soon, and Australia, Denmark and other countries have legalized it as well. We can benefit from their learning process and improve upon it.

Mr. Chairman, when Evan Bayh became Governor of Indiana in 1989, he did not support gambling, but the people spoke and voted for a repeal of our Constitutional ban on gambling. Soon, lawmakers passed a state lottery followed by riverboat gambling. Governor Bayh concluded that if gambling was to be legal in Indiana, he would appoint people of unquestionable integrity to head up the regulatory effort. He appointed a federal prosecutor as the Executive Director of the state gaming commission and the commission passed tough regulations and made clear from the outset that tough enforcement would be used against any law violators. As a result, we had a remarkably clean operation from Day One. The federal government should also acknowledge now that Internet gaming will continue to grow in America and we should appoint tough, fair-minded people with integrity to develop model approaches and help establish international standards for Internet gaming regulation.

In summary, I do not believe that the choice before this subcommittee is whether or not there will be Internet gambling in the U.S.—there most certainly will be. The question is what sort of Internet gambling there will be. Under H.R. 21, it will be an unlicensed, unregulated industry where the federal and state governments afford no protection to players, to minors or to problem gamblers, and it will be funded by less-than-transparent transactions, with no economic benefit or tax revenue accruing to the U.S. Under H.R. 1223, there is the potential for a tightly-regulated industry overseen by Americans of integrity bolstered by laws and regulations that provide substantial protections for minors and problem gamblers, remove any potential for money laundering, and provide economic benefit and tax revenue in the United States.

Once again, I thank you for the opportunity to testify, and I look forward to the question and answer session.

Mr. COBLE. Thank you, Mr. Modisett. I appreciate that.
Mr. Hornbuckle.

**STATEMENT OF WILLIAM J. HORNBUCKLE, PRESIDENT AND
CHIEF OPERATING OFFICER, MGM MIRAGE ONLINE**

Mr. HORNBUCKLE. Thank you, Mr. Chairman.

Mr. Chairman, distinguished Members of the Committee, thank you for inviting me today to testify about the MGM MIRAGE position on Internet gaming.

I am Bill Hornbuckle, President and Chief Operating Officer of MGM MIRAGE Online, a wholly owned subsidiary of MGM MIRAGE, with head offices in the Isle of Man and Las Vegas, NV.

MGM MIRAGE is one of the world's leading and most respected entertainment, hotel, and gaming companies that owns and operates 15 casino resorts located in Nevada, Mississippi, and Michigan. We employ more than 43,000 men and women, we manage \$10 billion in assets, and generate over \$4 billion in revenue annually.

Since all of our casinos operate under privileged gaming licenses, we clearly understood what was at stake for our company and the industry when we decided to pursue online gaming and seek the appropriate licensing. In September of 2001, MGM MIRAGE was awarded one of three online gaming licenses from the Isle of Man. Our site went live in September of 2002 and has been accepting wagers from a small number of Western European countries.

I am here to testify today in opposition of H.R. 21. Given the need to be brief, and the extensive nature of this subject, I have made an additional submission of supplemental material that cover the interactive gaming market, operations, regulations, and anti-money laundering code that govern our activity. While this mate-

rial is voluminous—and I do apologize for that—I thought it important to share with all stakeholders before any legislation was passed.

My message today centers around the following three basic premises:

Premise one. H.R. 21 will not stop Internet gaming in the United States. We strongly suggest that prohibition in the United States has a long list of failures associated with it. Any attempt of prohibiting activity on the Internet, gaming or otherwise, will unfortunately suffer a similar fate. We see this activity as ubiquitous and impossible to control from an end-user perspective, with long-term attempts to do so as futile.

The commercial reality in the United States is that every major financial institution has ceased taking credit and debit card transactions for online gaming. Despite the banking industry's preemptive move last spring, the recent General Accounting Office report stated that the online gaming industry would grow to \$4.2 billion in 2003, at a growth rate of 20 percent. Nothing proposed in H.R. 21 will stop that growth. This bill will have limited impact on a very resilient industry.

Bets from America are prohibited on the MGM MIRAGE site; yet, without any promotion, more than 60 percent of all registration attempts are from U.S. citizens, none of which have made it through our rigorous player protection system. America is playing online. They are now simply doing it offshore in unregulated markets.

Premise number two: the law of unintended consequences of H.R. 21 is in direct contrast with the things it seeks to stop. The bill would push offshore all regulatory and probity issues of a product that is a click away from 110 million Internet users in America. H.R. 21 will do nothing to protect these consumers.

State gaming regulatory bodies and Federal law enforcement agencies, which have been effective in the past in controlling gaming, will be prevented from regulating an activity that remains a click away. Further, by eliminating all regulated and credible financial institutions, you have encouraged an e-commerce market that is ripe for money laundering.

Premise three: you can properly regulate online gaming. Unlike just a couple of years ago, the tools and business methodology exist today to effectively regulate this industry. The support material we have provided highlights that the four key issues most commonly associated with online gaming—jurisdictional control, age verification, responsible gaming, and money laundering—can be properly administered.

Although no singular technology solution is perfect, MGM MIRAGE, through our geo-verification module, has been able to leverage database queries on customer location, residence, age and fraud detection. After several thousand registration trials and numerous attempts by regulators through State controlled testing labs, we believe we have successfully blocked all inquiries from nonviable jurisdictions and users who are underage.

We urge you to consider the merits of H.R. 1223, which calls for an Internet Gambling Licensing and Regulatory Study Commission. Only through research and study can sound and effective leg-

islation be drafted, passed and enforced. In order to determine the best way to protect the public's interest, we are strongly suggesting that further study needs to be completed on this complex subject before any law is enacted upon.

The public, which clearly enjoys this activity, is deserving of proper protections from operators who are held only to the highest standards. The debate should not center on how do we prohibit on-line gaming, but rather, now that online gaming is in American homes to stay, how do we effectively regulate and control it. This activity simply cannot be legislated away.

Again, I thank you for allowing me to testify. I would be pleased to answer any questions you may have on this matter today or in the future.

[The prepared statement of Mr. Hornbuckle follows:]

PREPARED STATEMENT OF WILLIAM J. HORNBUCKLE

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I am Bill Hornbuckle, President and Chief Operating Officer of MGM MIRAGE Online, a wholly owned subsidiary of MGM MIRAGE, with head offices in the Isle of Man and Las Vegas, Nevada.

MGM MIRAGE is one of the world's leading and most respected entertainment, hotel, and gaming companies that owns and operates 15 casino resorts located in Nevada, Mississippi, and Michigan. We employ more than 43,000 men and women, manage 10 billion dollars in assets and generate over 4 billion dollars in operating revenues annually.

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We see this activity as ubiquitous and impossible to control from end-user perspective, with long-term attempts to do so as futile.

The commercial reality in the United States is that every major financial institution has ceased taking credit and debit card transaction for online gaming. Despite the banking industry's preemptive move last spring, the recent General Accounting Office report stated that the online gaming industry would continue to grow to 4.2 billion dollars in 2003 at a growth rate of 20 percent.

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The bill would push offshore all regulatory and probity issues of a product that is a click away from 110 million Internet users in America. H.R. 21 will do nothing to protect these consumers.

State gaming regulatory bodies and federal law enforcement agencies, which have been effective in the past in controlling gaming will be eliminated from regulating an activity that remains a click away.

Further, by eliminating all regulated and credible financial institutions, you have encouraged an e-commerce market that is ripe for money laundering.

Premise 3. You can properly regulate online gaming.

The tools and business methodology exist today to regulate this industry. The support material we have provided highlights that the four key issues most commonly associated with online gaming; jurisdictional control, age verification, responsible gaming, and money laundering can be properly administered.

Although no singular technology solution is perfect, MGM MIRAGE through our geo-verification module has been able to leverage database queries on customer location, residence, age and fraud detection. After several thousand registration trials and numerous attempts by regulators through state controlled testing labs, we believe we have successfully blocked all inquiries from non-viable jurisdictions and users who are underage.

We urge you to consider the merits of H.R. 1223, which calls for an Internet Gambling Licensing and Regulatory Study Commission. Only through research and study can sound and effective legislation be drafted, passed, and enforced.

We are strongly suggesting today that further study needs to be completed on this complex subject before any law is enacted upon.

The debate, should not center on how do we prohibit online gaming, but rather now that online gaming is in American homes to stay, how do we effectively regulate and control it.

This activity simply cannot be legislated away.

Thank you again for allowing me to testify today. I again would encourage you to review the material submitted. I would be pleased to answer any questions you may have on this matter today or in the future.

Mr. COBLE. Gentlemen, the Members of the Subcommittee thank you, express our thanks to each of you, for this contribution. Let me start with Mr. Malcolm.

Mr. Malcolm, some have said that the way H.R. 21 is drafted, it could be interpreted as a weakening of the Wire Act. Do you agree with this statement (a), and could you give us an example of how this could weaken that statute?

Mr. MALCOLM. Certainly, Mr. Chairman.

It weakens it in a couple of rather subtle ways. The main one perhaps deals with section 3(c)(4)(B) of the bill, which I would contend presents a carve out for Internet service providers for liability under section 1084. That section essentially says that before an ISP can be held liable under the Wire Act, one must prove a violation of this law and, in addition to that, one would have to prove that the ISP not only had knowledge of the bets or wagers being placed, but in addition to that, also had to own, operate or control the gambling website in question.

That increases the quantum of proof that the Government would have to offer against an ISP under 1084, well above that which would be established under an aiding and abetting theory. For example, if an ISP were taking money for advertising for an Internet gambling site, clearly connecting supply and demand, with knowledge that that is what they were doing, even if you put the ISP on notice, and even though they were clearly facilitating this gambling activity, they would not longer violate 1084. They would say well, we have knowledge of the bet or wager, but we don't own, control or supervise the Internet gambling website. Therefore, they would be carved out of 1084.

There are some other brief anomalies dealing with the definitional sections between this section and 1084, but we can deal with the staff on that.

Mr. COBLE. All right. Thank you, Mr. Malcolm.

Mr. Hornbuckle, I have been asked by my colleague from Utah, Mr. Cannon, to ask this question that is peculiar to his State of Utah.

Utah law prohibits gambling. Could you technologically prevent people in Utah from gambling on the Internet? If so, how would you do that?

Mr. HORNBUCKLE. Mr. Chairman, yes, we could.

When we went forward with licensing, as you know, we're privilege licensed in the States I mentioned earlier. Nevada, of note, where most of our assets reside, made us commit to and we created technology that, if a country has made gambling illegal, or specifically made Internet gambling illegal—and I'll use the case of Japan, where gambling is illegal, and Hong Kong, where Internet gambling is illegal—we have put forth in our system through IP blocking and other methodologies, which are laid out here, a system that says "no, you cannot get in". It has been 99.9 percent effective in doing that.

No system is perfect, but we can deliver with reasonable assurance to the Congressman that the folks from Utah, if he didn't want them in, wouldn't be put in.

Mr. COBLE. All right. I'll convey that to him.

Mr. HORNBUCKLE. Thank you.

Mr. COBLE. Mr. Leach, we know that you have been involved in this issue for a long time. Some believe that Internet gambling should be licensed and regulated rather than prohibited, as we have heard today. Can you tell us, based upon your years of investigating this issue, whether or not licensing and regulating is a realistic alternative to prohibition, and why?

Mr. LEACH. Well, certainly you can license and regulate. The question is, is it good for the country? Is it good for the individuals involved? I think, when you go to the individual, you have this dilemma of do you want to turn the home into a casino, where there is virtually no constraints, particularly in people that appear, as has been described by the medical profession, in an almost quasi-genetic way, where one-and-a-half to 2 percent of Americans, once they start to gamble, it's pretty hard to stop. You have working in the home less constraints than you would have in going to an actual casino. I think you would open that problem up rather dramatically. In addition, you keep all the social problems that currently exist, with a single positive of—you have to recognize that there is good and bad to almost any proposal, where you would probably bring a little more gambling onshore. But if one has real doubts about the individual and social implications of Internet gambling, then I don't think that would be a wise way to go.

I would make one final comment, because it relates to the very thoughtful testimony of someone who has a different judgment than mine from MGM. When they say there's no consumer protection, the ultimate consumer protection is that the consumer will not have to pay an Internet gambling debt if he cannot use a financial instrument. So the lack of ability of a casino that's on the Internet to take the losses, which are virtually assured over any period of time, will protect the American consumer maximally.

Mr. COBLE. Thank you, sir. I see that my time has expired.

The gentleman from Virginia.

Mr. SCOTT. I had one technical question. On page 6 of the bill, Mr. Malcolm, of H.R. 21, line 15, it says that one of the things it exempts is "any lawful transaction with a business licensed or authorized by a State."

Does that exempt lotteries? It's page 6, line 15.

Mr. MALCOLM. If I may have just a moment. [Examining.] Absolutely, Mr. Scott.

Mr. SCOTT. Okay.

Mr. Malcolm, you indicated that there are 1,800 sites now. Are those 1,800 accessible from the United States that you're talking about?

Mr. MALCOLM. Well, it's possible there are a handful of sites, such as Mr. Hornbuckle's site for the MGM MIRAGE, where they may be able to successfully block access to the United States. But by and large, the Internet is an open territory where one can route computer communications through any country. I would think that, with a little ingenuity by a tech-savvy person, yep, they would all be available.

Mr. SCOTT. Mr. Hornbuckle, you said you could block out a Utah address. If someone calls a long distance number to kind of log in, how would you know they were physically in Utah and not in Nevada?

Mr. HORNBUCKLE. Through IP mapping, through a product we use called QUOVA, you can not only identify the origin, you can tell if they're using an anonymizer. It's a layered weighted system that tells you if it's direct or dial up.

Based on those indicators and other things that layer into the approach we take, in terms of banking institutions, address, voter registrar, you know, we go back and check data queries and we can determine with reasonable assurance where they're coming from.

Mr. SCOTT. You can verify the residence of the name of the person the account is in?

Mr. HORNBUCKLE. That's correct.

Mr. SCOTT. You would have no way of knowing whether or not that named person is, in fact, the one doing the gambling?

Mr. HORNBUCKLE. That's correct, other than there is a pin code that goes back to the customer through the regular mail. To the extent they have that pin code, that's the identification we have on the other end.

Mr. SCOTT. How do you deal with responsible gaming?

Mr. HORNBUCKLE. There is a player protection module on our site, which I have identified and laid out in great detail in the material we have submitted. It enables a potential customer to go online and limit their stake activity in terms of time, amount wagered, deposits, or withdrawals for that matter. It's a device that enables them to monitor what their own play activity is, as well as we can monitor it if we choose to.

Mr. SCOTT. Mr. Malcolm, are gambling debts enforceable under this bill? I know in Virginia, at least the law used to be that you couldn't legally collect a gambling debt. Would this scheme affect any of that?

Mr. MALCOLM. Under H.R. 21, there are civil remedies, including the ability to essentially freeze an account to prevent any financial

activity going to and from that operation. If you're asking as a matter of civil law whether you can collect on a gambling debt, generally one can't collect on unenforceable or illegal contracts. But, you know, that's not my area of expertise particularly.

Mr. SCOTT. Mr. Modisett, you indicated ways of evading this H.R. 21. Could you go into a little more detail about that? You mentioned wire to an offshore bank, escrow accounts, I assume long-distance calls into an Internet provider, and using an access number in Canada would be another way?

Mr. MODISETT. Yes. Actually, you're listing all of them there as an example, the point being that you want transparency to be able to follow these transactions. Credit cards are one of the best ways to have that sort of transparency. So when you start closing down that aspect of the financial transaction, like the balloon, it's going to spread out into other areas. They will find ways to go ahead and gamble. Those other ways that you cited will be less transparent and more difficult to follow, and to the extent there is a potential for abuse, my concern is that that is going to worsen the problem rather than make it better.

Mr. SCOTT. Mr. Hornbuckle, who regulates your site to make sure that the odds that people think they're playing against are, in fact, the odds?

Mr. HORNBUCKLE. The actual licensing is with the Isle of Man government, but we also have made submissions of our license in our games to the other jurisdictions that we operate in—Mississippi, Nevada, New Jersey and...I'm missing one.

Mr. SCOTT. Who gets the tax benefit on the profits?

Mr. HORNBUCKLE. The Isle of Man government.

Mr. SCOTT. Does the United States get any benefit from that?

Mr. HORNBUCKLE. No, they do not, because we do not accept U.S. wagers at this time.

Mr. COBLE. Mr. Hornbuckle, I didn't hear the last thing you said to Mr. Scott.

Mr. HORNBUCKLE. I'm sorry. No, they do not. He asked if the U.S. was any beneficiary from taxes, and the answer is no, nor are other jurisdictions, other than the Isle of Man, because we do not take U.S. bets at this time.

Mr. COBLE. Very well. Thank you.

Mr. Feeney, the gentleman from Florida. Were you through, Bobby?

Mr. SCOTT. Yes, thank you.

Mr. FEENEY. Thank you, Mr. Chairman.

Mr. Hornbuckle, do you have any estimates, either your company or the industry, do you have any estimates of what percentage of Internet gambling is run through companies like yours, that have submitted their odds that Mr. Scott asked about, for example, to Mississippi, New Jersey and Nevada, and what percentage is completely unregulated at the present time?

Mr. HORNBUCKLE. I would suggest to you that all operators, where they have their jurisdiction and licensing regimes, would tell you that they're regulated. So I think it's a matter of what you would consider regulation.

What we go through in the Isle of Man and what ultimately holds us to our standard based in Nevada and all that we have at

stake, is a different bar and a bar we all ought to get to, and potentially what happens in a Caribbean country. But they would tell you that they are regulated. Our games are out there, registered with the Isle of Man government, within certain standards that they call out, and we have to adhere to those standards.

Mr. FEENEY. What you have suggested without saying it is that some of your competitors may not have the integrity that MGM does. I guess my question would be, what percentage of the Internet gambling today is with less credible entities than MGM, in your opinion?

Mr. HORNBuckle. With all due respect, sir, I would like to hold comment on that. [Laughter.]

I couldn't accurately give that estimation anyhow.

Mr. FEENEY. Maybe Mr. Malcolm has an opinion about that.

Mr. MALCOLM. My guess, Mr. Feeney, would be that a whole bunch of them are less scrupulous and less honorable than MGM MIRAGE.

Mr. FEENEY. Assuming that most consumers in America are reasonably wise, that would suggest the addictive tendencies of Internet gamblers to me, anyway, because to the extent that I want to be entertained for a reasonable value for my buck and I want some reasonable odds in return, I'm probably going to pursue regulated places to gamble, where I can be assured of a fair square deal, even though I understand it's ultimately in the house's advantage.

Isn't this suggestive that Internet gamblers behaviorally, Mr. Hornbuckle, may tend to be more addictive and less responsible gamblers?

Mr. HORNBuckle. I don't know that it suggests it's more addictive. I will tell you that the commercialities of odds and what goes on in the Internet world at large are such that, to be competitive and to survive, nobody is taking huge advantage of customers out there, or they won't.

Gamblers are savvy, particularly the ones that are on line. To the extent they then ultimately get compensated for their wagers and their winnings, if they have some—and they do have some—I think speaks to the credibility of who the operator is. That's where you get into issues of are they licensed, are they credible, is a brand like MGM MIRAGE meaningful or not. That's something that would ultimately be up to the general public to decide.

Mr. FEENEY. I would like to ask my colleague, Congressman Leach, if he has an opinion about the elasticity of demand for gambling as it relates to Internet opportunities

Our staff estimates that, in the last 10 years, we have had roughly a ten-fold increase in American dollars wagered over the Internet. I would like to ask my colleague if he's got an opinion. Does that come at the expense of gambling on things like lotteries, regulated casinos, gambling ships, penny ante games and office pools, or is this increase likely to be in addition to all the above? Not to mention pork belly futures on the mercantile market.

Mr. LEACH. Well, I'm not an expert. Frankly, the competitive aspect would be better asked of someone from MGM that would know that better than I.

I would say there are two things that stand out. One is the terrific growth in the Internet. Clearly, there is some competition with casino gambling. How big that is, I don't know.

Secondly, the fact is that there are lots of studies of the gambling issue, per se. Your National Commission on Gambling went into some of this, which shows that there is part of America that really does get hooked in analogous ways to alcohol or drugs, and then some correlation between the two. That is, if one is likely to be hooked on a drug or alcohol addiction, one is as little more likely to be an addictive gambler. But the key thing is, one can quite quickly and rapidly lose a great deal.

Certainly there is a case, as MGM has made, that it would be better if you were to deal with a reputable company versus less reputable. But I think the more compelling case is to deal with nobody.

I would defy anyone on this panel to give me a strong social case for Internet gambling. I mean, what is it? Is there a national interest case for it? Is there an individual family case for it? And then to think in reverse terms, are there some disadvantages to the country, some disadvantages to the individual? I think it gets pretty compelling.

Mr. COBLE. The gentleman's time has expired.

The gentlelady from Texas.

Ms. JACKSON LEE. Thank you very much, Mr. Chairman. I would ask unanimous consent that my opening statement be allowed to be submitted in the record.

Mr. COBLE. Without objection.

[The prepared statement of Ms. Jackson Lee follows:]

PREPARED STATEMENT OF THE HONORABLE SHEILA JACKSON LEE, A REPRESENTATIVE
IN CONGRESS FROM THE STATE OF TEXAS

I would like to thank Chairman Coble and Ranking Member Scott for convening this very important hearing today.

We are here today to hear testimony and discuss two bills related to Internet gambling—H.R. 21 and H.R. 1223.

There have been attempts in the last two Congresses to outlaw internet gambling, or in the alternative to restrict internet gambling such as restricting how bets are made. The bills we are considering today are continuation of those prior efforts.

H.R. 21 prohibits internet gambling businesses from accepting bets from credit cards, electronic fund transfers, money transmitting business transfers, and instruments or transactions drawn through financial institutions. It also grants Federal district courts jurisdiction over violations of bill, requires the Secretary of the Treasury to prescribe regulations on payment systems and policies to prevent restricted transactions, and calls for U.S. and foreign governments to cooperate to prevent money laundering and other crimes.

The issue of internet gambling is always debated vigorously. The Internet gambling industry receives wagers amounting to an estimated \$4.2 billion dollars per year through 1,800 internet gambling sites. Internet gambling has a high likelihood of causing personal bankruptcy, provides a fertile ground for fraud and money laundering, is difficult for states to regulate, and offers an addictive and appealing gambling outlet for children.

I was an original co-sponsor of H.R. 3215, an internet gambling bill considered in the last Congress, because of my grave concern that children and teenage gamblers, who have wide access to the Internet, will abuse the Internet for gambling. A study released by the American Psychological Association finds that pathological gambling is more prevalent among youths than adults. Between five and eight percent of young Americans and Canadians have a serious gambling problem, compared with one to three percent of adults. The study went on to say that with gambling becoming more accessible in U.S. society, it will be important to be able to intervene

in children's and adolescent's lives before the activity can develop into a problem behavior.

Many Internet gambling sites require bare minimum information from gamblers to participate. Security on bets placed over the Internet has proven ineffective. And unlike traditional regulated casinos, Internet operators have no demonstrated ability or requirement to verify a participant's age or identification. Also, an Internet gambling site can easily take a person's money, shut down their sites, and move on.

Gambling over the Internet, particular because of the danger it poses to our children, is a business that I simply cannot condone. Given the fact that the majority of our citizens have access to computers and the Internet, we must ensure that laws are in place to eliminate the potential harm of internet gambling.

While I am concerned about the impact of gambling, I am also concerned with protecting individual freedoms and personal choices. The freedom to gamble is such a choice. I look forward to hearing the testimony and comments by our speakers today in order to reconcile these issues. We must find a way to address this very serious problem of Internet gambling.

Ms. JACKSON LEE. I thank you very much, and I thank the gentlemen for their presentation, and Congressman Leach as well.

Over the course of my tenure in Congress, I have had the opportunity to be supportive of restrictions on Internet gambling, for a variety of reasons, but I think particularly on the issues dealing with money laundering, underage gambling, and gambling addiction, which permeate in many instances throughout the industry, regardless of whether it's Internet or person to person.

I do compliment the industry for being particularly sensitive to these issues over the years and working collaboratively with mental health groups and State groups on trying to prevent this. So I would like to find the best approach, the best reasonable approach to address a concern that will continue to grow with the utilization of Internet technology. Computer technology is growing, and we're going to find people doing everything with respect to computer software, and I think we have to be sensitive to that.

Let me ask Mr. Hornbuckle how much Federal regulation does the industry have now, just in general.

Mr. HORNBUCKLE. As it relates specifically to my activity on line, little to none.

Ms. JACKSON LEE. And overall?

Mr. HORNBUCKLE. Currently in our activity, it all comes out of the Isle of Man, and it is underwritten by what our code, what our licensing requirements are for places like Nevada and Mississippi, Michigan, et cetera. We have a great deal of respect for what we have there, so the way we conduct our business activity and the code that's called out, which I have included, both against anti-money laundering and the regs themselves from the Isle of Man govern our overall activity.

Ms. JACKSON LEE. So you're saying that you are registered under or incorporated under the Isle of Man. Are you're talking about all the MGM properties, for example, the ones in Las Vegas?

Mr. HORNBUCKLE. No, no, just for online activity. I'm sorry.

Ms. JACKSON LEE. Let me ask you to put on your other hat, just put on the hat for the overall. Tell me what kind of regulation it is for the overall business.

Mr. HORNBUCKLE. For overall business, we're probably one of the most licensed, if not the most licensed, industries in this country. From Nevada, Mississippi, New Jersey and Michigan, there's an extensive amount of licensing we go through, and probity, both as individuals and for our company. From understanding the Wire

money control Act, from understanding our customers, know your customer regimes, all of that activity goes on in our buildings. We have strict Reg 6-A requirements that we adhere to.

So, from a licensing perspective, and from a responsible gaming perspective, we have a full plate of things that we do that we look to bring to bear ultimately in this space.

Ms. JACKSON LEE. So by licensing, obviously that equates to regulation, that equates to, as I understand it, State law enforcement, who are pretty much knowledgeable about your business.

Mr. HORNBuckle. One hundred percent knowledgeable.

Ms. JACKSON LEE. In the respective States, whether it's Michigan, Mississippi or Las Vegas—

Mr. HORNBuckle. Correct.

Ms. JACKSON LEE.—you certainly are well-known and your business is well-known, and State legislators have regulated you, it is my understanding, correct?

Mr. HORNBuckle. That is correct.

Ms. JACKSON LEE. And you adhere to those regulatory requirements, which subject you to either civil and/or criminal penalties?

Mr. HORNBuckle. That's correct.

Ms. JACKSON LEE. This is a business that you would say has gotten more dynamic over the last how many years? I'm talking about Internet gambling.

Mr. HORNBuckle. The last two to 3 years specifically.

Ms. JACKSON LEE. And it brings in about how much money?

Mr. HORNBuckle. It's suspect, but our best guess is between \$4–5 billion and growing, growing particularly in Asia and Europe, as well as in the U.S. Despite the activity that has gone on over the last year, the U.S. continues to grow at about a 20 percent rate, we believe.

Ms. JACKSON LEE. Why the approach using the Isle of Man as opposed to the different jurisdictions that you're already in, the different States that you're already in?

Mr. HORNBuckle. Because of concerns for the Wire Act, and what is happening here in the U.S., we didn't think it prudent, given all that was at stake. We do not accept U.S. bets. We consider that off limits for now, and until this is made crystal clear to us, we will not accept U.S. bets.

The Isle of Man presented a jurisdiction that was very serious about money laundering. It has, much like Nevada is based on gaming, it is based on financial market sectors. They restricted their operation in taking U.S. bets, and they required all their operators to put up a two million pound bond to protect consumers. Those are some of the things that regulation would bring. We couldn't get licensed unless we put up two million pounds, that sits in trust for consumers if we decide to cease doing business.

Ms. JACKSON LEE. Do you think you're prone to more criminal activity, or have you surmised, or are you willing to give me the honest truth? Have you surmised a great deal of criminal activity in light of your present structure?

Mr. HORNBuckle. No. To the contrary. We are very focused on our business. We have so much at stake for this venture, we're very focused on our business.

Ms. JACKSON LEE. Let me talk to Mr. Malcolm at this point. As I indicated, I have been supportive, but I would think—Mr. Chairman, would you yield me an additional minute?

Mr. COBLE. One additional minute.

Ms. JACKSON LEE. Thank you.

I have noted that the Department of Justice has its hands quite full. What component with the Wire Act, I know, and what other aspects of the gambling industry here in the States do you regulate presently?

Mr. MALCOLM. Specifically, there are——

Ms. JACKSON LEE. Federal jurisdiction. That's what I mean.

Mr. MALCOLM. There are several Federal statutes that cover this particular topic. The Wire Act is only one of them. The Wire Act makes it a crime to transmit in interstate or foreign commerce bets on——

Ms. JACKSON LEE. Existing. These are existing——

Mr. MALCOLM. Right. In 1952, the Travel——

Ms. JACKSON LEE. I could run through them rather quickly because my time is going to go, and I just want to——

Mr. MALCOLM. 1084, 1952, 1955, RICO could arguably apply. There are several other statutes.

Ms. JACKSON LEE. RICO I know could apply to what I would call person-to-person gambling, or the industry itself. Is there something in particular that—just forget about on-line. Do you regulate the industry, or do you interact with the States? You have specific laws to regulate the industry as it stands now, without online?

Mr. MALCOLM. I'm not sure of the interplay between the Federal regulators and the State regulators, but suffice it to say we work closely with them. Some of the Federal statutes are specifically enabled based on a violation of State law.

Ms. JACKSON LEE. Let me just comment on that. I appreciate it very much. I have always been one, when it comes to enhancing protection by utilizing the Federal authority, I am certainly open to it. I respect the work of Chairman Leach, but I perceive more potential confusion than not without a full appreciation of the impact of the prohibition on using credit cards and other vehicles, other bank instruments, to gambling on the Internet.

What I would propose, Mr. Chairman, and would think would be valuable, is to look carefully at 1223—additional 30 seconds, Mr. Chairman. I just want to close this sentence. What I'm concerned about, Mr. Chairman, is the fact that we need to study this question and understand it a little better, to see how the mix of State regulations, which Mr. Hornbuckle seems to be very much regulated on his regular gambling, and see how that works in order to tell us what is the best way to get to the point of prohibiting money laundering, underage gambling, and gambling addictions, versus the total prohibition, before we know what the facts are.

I thank the gentleman for yielding.

Mr. COBLE. The gentlelady's time has expired.

Folks, we have another hearing scheduled for this afternoon, but since there are only four of us here, I'm going to do a second round. Let's do a second round real quickly. I have three questions I want to put to you, and I am going to start with Mr. Malcolm.

Mr. Malcolm, I think you have some problems with the injunction provisions, do you not?

Mr. MALCOLM. That is correct.

Mr. COBLE. Is there a more effective way of drafting the injunction provisions of the bill?

Mr. MALCOLM. Specifically, I have problems with a couple of the injunction provisions. With respect to the ISPs, section 3(c)(4) imposes limitations on the relief that ISPs—that can be granted against ISPs. In addition, the websites themselves have ancillary services. But we're working with the industry to tinker with that.

More particularly, Mr. Chairman, there are limitations, there are various factors set forth in section 3(c)(5) of the bill. We believe that, while we recognize the important role the regulators have to play—and we're working with Treasury to ensure coordination—we object to the addition of any factors beyond the standard factors set forth in Federal Rules of Civil Procedure 65.

Mr. COBLE. Thank you.

Mr. Hornbuckle—strike that. Mr. Modisett, your argument, I believe, seems to suggest that to legalize Internet gambling seems to be based upon the size of the industry and the rate of growth that it's increasing. Some would suggest that it is not responsible for governments to legalize a criminal activity simply because it's growing or flourishing.

What do you say to that?

Mr. MODISETT. I would not say that my argument is based on the growth factor. I would say it is based on, first of all, the fact that those people who are playing, whatever the size, are currently in a highly unregulated environment. And I'm not referring to Mr. Hornbuckle's enterprise. I'm referring to those that are basically out of the Caribbean Islands and some of the other 1,800 that have been referred to here today.

I would like to drive those into a highly regulated space so that we have more control, more consumer protections, could impose preset loss limits, we could do a better job of making sure that minors aren't gambling, various other advantages that would come from this highly regulated regime.

My other concern is based on the fact that we have heretofore not jumped into an Internet space and called for an out-and-out prohibition, with the possible exception of such an obvious evil as child pornography. But with regard to something that is legal in some areas, not legal in other areas, this would be our first jump in, where we just out-and-out said that we are not going to allow an American business to have any financial transactions whatsoever.

I think that is a very big move, and it's a move that should take place only after further study.

Mr. COBLE. Good. Thank you, sir.

Finally, Mr. Leach. Some contend that Internet gambling is already illegal under the Wire Act and, therefore, this legislation is unnecessary. I'm not saying that. Some say it.

Comment on this, if you will, and explain why your bill is necessary?

Mr. LEACH. I accept the premise that I believe the Wire Act covers Internet gambling, although some court jurisdictions have gone

to the contrary. But what our bill does—and it's carefully crafted to fit into whatever your Committee does—it is an added enforcement mechanism of whatever the law is at any point in time. So if you want to expand or contract the law, that's the jurisdiction of this Committee with the Congress. But all we do is add an enforcement mechanism.

It happens, and it's really a bizarre fact of how the private sector interrelates with the public, that the public has had virtually no capacity to enforce this, so your Department of Justice can testify that there are all these gambling sites but it cannot testify that it has terribly effectively shut them down. I'm not saying that the fault of the Department of Justice. All I'm saying is that that's a circumstance.

The approach of this bill is designed simply to serve as a functional deterrent, based on enforcement utilizing the private sector. Let me tell you, it has taken a lot of effort to get acceptability or consensus, as grudgingly as it may be, because you're putting a new obligation on the private sector, a private sector that principally the Financial Services Committee interrelates with more than other Committees of the Congress.

I personally accept the broad interpretation that the Justice Department has applied, that the Wire Act does apply to Internet gambling, but there is no precise reference in the Wire Act to that, so it's a broad interpretation of intent, I think, would be the description, as a nonlawyer having the disadvantage of addressing all of you that are better educated.

Mr. COBLE. Thank you, Mr. Leach. I see my red light is about to appear.

The gentleman from Virginia.

Mr. SCOTT. Thank you, Mr. Chairman.

The gentleman from Iowa indicated or asked us to make the social case for Internet gambling. Frankly, I think it's a difficult case to make, but that's not the question before us. I think the Justice Department official, Mr. Malcolm, has indicated that it's already out there, so the question is what are you going to do.

This bill, H.R. 21, doesn't prohibit Internet gambling. It makes it a little more administratively challenging to place the bet, but as we've heard, not impossible and not even that difficult, after you do a little investigation. So the social case isn't the question before us. The question is what to do about reality.

I would ask Mr. Hornbuckle, can you access your site from outside of the United States, anywhere outside of the United States?

Mr. HORNBUCKLE. There are about ten countries that we accept wagers from. UK is our principal market, though, by example.

Mr. SCOTT. Canada?

Mr. HORNBUCKLE. No.

Mr. SCOTT. Mexico?

Mr. HORNBUCKLE. No. Mostly Western Europe, South Africa, New Zealand, principally in Western Europe and a couple of Scandinavian countries.

Mr. SCOTT. Now, you pay off your bets because your reputation would be at stake if you didn't. The problem with websites is you can create a website today and shut it down tomorrow afternoon. If we don't regulate it, what prohibition would there be, or how

would you deal with a website that sets up, takes a lot of money, and then just closes down? What remedy would a gambler have if that happened?

Mr. HORNBUCKLE. In today's environment—I can think of three sites over the most recent Super Bowl, where the underdog won and it closed. I know it's reality, but they did, in fact, close. To my understanding, those people were left unpaid.

In the Isle of Man, or in any regulated environment—in our example of the Isle of Man, we are bonded for two million pounds. That's what that money is for. To the extent we went out of business, or anybody else would go out of business, there would be reserve funds to take care of those people.

Mr. SCOTT. Does the two million pounds, how does that compare to the money that's coming in and out?

Mr. HORNBUCKLE. Right now, the money that comes in and out on an ongoing basis, that we hold in balance, where people leave an account, it's maybe 5 percent of that number. It's not—and it's monitored constantly by the government. To the extent it approaches it, they have reserved the right to look at that number again.

Mr. SCOTT. So that you would be bonded for the amount that would be owed if you went out of business?

Mr. HORNBUCKLE. That's the theory behind it, yes. Obviously, it's a new industry, but that is absolutely the theory behind that bond.

Mr. SCOTT. And if somehow I got access to a fancy looking website and gambled and happened to win, and they went out of business, if they were unregulated I would have no recourse?

Mr. HORNBUCKLE. That's correct.

Mr. SCOTT. Thank you, Mr. Chairman.

Mr. COBLE. Thank you.

The gentleman from Florida.

Mr. FEENEY. Mr. Hornbuckle, when it is your physical casino at MGM, you entertain "high rollers". Do you pre-qualify them with credit applications and verification, the same way a banker would do?

Mr. HORNBUCKLE. In some instances, that's correct.

Mr. FEENEY. Do you do that with any of your Internet gamblers as well?

Mr. HORNBUCKLE. Yes, we do. Again, the documents that we submitted, under the money laundering provisions, anybody who puts over a thousand dollars on deposit has got to then give to us copies of either a passport, national ID, or some other form of ID that the Government has specified. So the answer is, at that level or above, it's not identical but close in principle to what we do in highly regulated markets like in Nevada.

Mr. FEENEY. But presumably, if we did not disallow or prohibit financial institutions from providing credit to gamblers, presumably there would be no prohibition from somebody without the ability to comfortably lose a significant sum of money, \$500 or \$1,000 or more. There would be nothing to require the casino or the financial institution, other than the credit limit on their credit card, to regulate whether or not this was a prudent amount of money for somebody to be putting down on a game of chance.

Mr. HORNBUCKLE. In an unregulated market, I would have to agree with that. In a regulated market, at least you have an opportunity to get into that discussion. I guess that could be said about many things in life as well. I mean, this happens to be gaming, but I think regulatory restrictions on that are key.

Mr. FEENEY. I guess I wanted to ask Congressman Leach, because I'm very sympathetic toward the goals of H.R. 21. But it does seem to me that in certain types of high risk investments, for example, the SEC and other regulators require that the sellers and the marketers of the instruments, they are a very high risk insurer that is only a small percentage of the net worth of the individual that's being put into this high risk venture.

Isn't there an opportunity through regulation that doesn't exist through prohibition to sort of, you know, protect people from themselves?

Mr. LEACH. Well, I think you can provide a modicum of protection. You know, that's clear. Whether that protection is very significant in relationship to the broad scope of the problem is a matter of individual judgment. I would fully acknowledge that there are advantages to some types of protection relative to no types of protection, but I believe the subject matter in general is one that, if you can't make a social case for it, what difference does it make if you have a little more protection? So I don't find it a compelling concern. Certainly, parts of things that MGM would propose today are quite respectable.

Mr. FEENEY. I think that's a fair admission. I mean, certainly we have a lot of seniors in Florida, and some of them have been to the dog track every day of their adult lives. They get to a point where they can't drive, can't travel, and if somebody with a net worth of a million dollars wants to bet \$20 on the third race every day at Calder from his living room, I don't think you're suggesting that that is necessarily anti-social or dangerous behavior.

Mr. LEACH. I think there are examples where one could find this is quite a tolerable circumstance. There are also examples where one would say this is truly tragic for the individuals involved.

Mr. FEENEY. Mr. Modisett, or maybe Mr. Malcolm as well may want to answer this last question. The ingenuity and creativity and the technical skills of young people never ceases to amaze me. They are able to break into Pentagon-secure matters and they are able to turn upside down the whole computer networks of corporations. My oldest son is just 10, but at some point, if he wants to get into my credit card system and my computer system and avail himself, I have no doubt that he or somebody like him, at age 14 or 16, will have all of the knowledgeable capabilities necessary.

How do you deal with the issue that, at least if he tries to enter a casino, somebody is going to have to look him in the eye and presumably be responsible for physically carding him, physical security, et cetera. How do you answer the question that there simply is no way to regulate what goes on inside that house with people under age? It's not addicts, necessarily, but people who are not able to lawfully consent to the contract.

Mr. MODISETT. I think that with regard to actual computer hackers, those that are quite proficient at getting around particular systems, as Mr. Hornbuckle said, there is no foolproof way that you

could say 100 percent to keep them out. But I would say that the instance with regard to Internet gaming would be no worse than it would be with regard to any other activity on the Internet.

There is technology out there—and MGM has referred to some of it—that is about as foolproof as you can get in modern society and high technology. I would rather see a piece of that sort of technology—I was advising at one point another company that was skill-based, so it wasn't wasn't gaming but was skill-based on the Internet. They had the technology, and others do now, to make sure that no juveniles were using it. They had preset limits so that no one could go over a particular amount, the sort of regulation that you would like to see instead of it being the "wild west", which we have, with regard to too many of these Internet gaming sites now.

Mr. MALCOLM. May I briefly respond, Mr. Feeney?

I think you hit the nail on the head. While perhaps there is software out there that is as good as it can be, my understanding is that that software is far from perfect. In addition to that, software is easily manipulable. If you have a physical location where a minor has to go, they can get proof of identification, they can eyeball that person. This is not a hypothetical problem. One in ten boys, every month, is engaging on a monthly basis in Internet gambling. College students, who have recently gotten credit cards but have no money, are up to their eyeballs in debt because they're spending all night on online gaming poker situations.

Mr. MODISSETT. If I could just add to that, Mr. Congressman, I was chair of the Indiana Gambling Impact Study Commission, and when we did our poll, we also asked questions about Internet gaming among youth. We came up with 0.4 percent that had said they had even attempted to gamble on the Internet. So—

Mr. MALCOLM. I would just refer to—There's a study coming out by the Annenberg Public Policy Center at the University of Pennsylvania, and that's where I got that statistic from.

Mr. COBLE. The gentleman's time has expired.

Mr. Scott?

Mr. SCOTT. Mr. Chairman, I would ask Mr. Malcolm if he would be willing to respond to questions in writing, particularly about the section that I indicated, and I think the Ranking Member of the Committee has some questions about that section.

Mr. MALCOLM. I would be delighted to, Mr. Scott.

Mr. SCOTT. With that, Mr. Chairman, I would ask unanimous consent that the hearing record be kept open until at least the mark up on either of these bills.

Mr. COBLE. And I would also say that any Member of the Subcommittee who wanted to submit written requests, that would be in order.

Gentlemen, we thank you all for your contribution today. This concludes the hearing and we appreciate your contribution.

The record will remain open for 1 week. Thank you for your cooperation. The Subcommittee stands adjourned.

[Whereupon, at 3:20 p.m., the Subcommittee adjourned.]

A P P E N D I X

MATERIAL SUBMITTED FOR THE HEARING RECORD

PREPARED STATEMENT OF THE HONORABLE HOWARD COBLE, A REPRESENTATIVE IN
CONGRESS FROM THE STATE OF NORTH CAROLINA

Today, the Subcommittee on Crime, Terrorism, and Homeland Security addresses a serious and growing problem for our Country. The problem of Internet gambling. It is now estimated that \$4.2 billion is wagered over the Internet each year. This is an increase from \$445 million just six years ago. There are currently more than 1,800 Internet gambling sites, and the total dollar amount wagered worldwide is expected to reach \$10 billion in the near future.

The most troubling aspect of Internet gambling is the relative ease of accessibility for our nation's children. The anonymous nature of the Internet makes it almost impossible to prevent underage gamblers from using their parents' credit cards, or even their own in some cases, to log on to a gambling website. Many Internet sites require nothing more than a name, address, and credit card number. Those sites that do require a person to disclose his or her age make little or no effort to verify this information.

Another group of people particularly susceptible to Internet gambling are America's problem gamblers. The National Council on Problem Gambling estimates that there are currently eleven million Americans directly suffering from gambling problems. High rates of financial debt, unemployment, bankruptcy, divorce, homelessness, and suicide are all associated with problem gambling. Virtual casinos and their video game structure have been labeled the "crack cocaine of gambling." These facilities are open twenty-four hours a day, seven days a week, all within a person's own home. By making gambling more convenient, it can do nothing but make the problem worse.

In addition to the social problems associated with Internet gambling, these Internet sites also offer organized crime groups a very simple and easy opportunity to launder the proceeds of their criminal activity. Because of the lack of oversight or regulations and the high degree of anonymity, money laundering through Internet gambling sites is already a major concern to our nation's law enforcement agencies.

Federal law is currently unclear as to whether or not all types of Internet gambling is illegal. The statute that most directly restricts the use of the Internet to place bets is the "Wire Act" under section 1084 of Title 18 of the U.S. Code. However, because this statute was written before the age of the Internet and the use of wireless communication, there is ambiguity as to what type of betting is or is not covered. Also, the types of gambling mentioned in the statute may not cover all of the different types of gambling available on the Internet.

Today we will examine two bills that attempt to address the problems of internet gambling in two very different ways. H.R. 21, the "Unlawful Internet Gambling Funding Prohibition Act" introduced by Congressman Jim Leach of Iowa, seeks to ban Internet gambling by prohibiting the use of financial instruments, such as credit cards, in any transaction involving illegal Internet gambling. H.R. 3215, the "Combating Illegal Gambling Reform and Modernization Act" introduced by Congressman John Conyers of Michigan, seeks to establish a commission to study the feasibility of regulating Internet gambling rather than banning it.

I look forward to the testimony of the witnesses here today which will help this Subcommittee decide what is the best approach to take with regard to this very important subject.

PREPARED STATEMENT OF THE HONORABLE BOB GOODLATTE, A REPRESENTATIVE IN
CONGRESS FROM THE STATE OF VIRGINIA

Thank you Mr. Chairman for holding this very important hearing. I would like to commend my colleague, Congressman Jim Leach, on his tireless efforts to address the problem of Internet gambling.

The Internet is a revolutionary tool that dramatically affects the way we communicate, conduct business, and access information. As it knows no boundaries, the Internet is accessed by folks in rural and urban areas alike, in large countries as well as small. The Internet is still expanding by leaps and bounds and more and more citizens are logging on to the Internet at home; however, it has not yet reached its full potential as a medium for commerce and communication.

One of the main reasons that the Internet has not reached its potential is that many folks view it as a wild frontier, with no safeguards to protect children and very few legal protections to prevent online criminal activity. The ability of the World Wide Web to penetrate every home and community across the globe has both positive and negative implications—while it can be an invaluable source of information and means of communication, it can also override community values and standards, subjecting them to whatever may or may not be found online. In short, the Internet presents a challenge to the sovereignty of civilized localities, States, and nations to decide what is appropriate and decent behavior.

Gambling is an excellent example of this situation. Gambling is currently illegal in the United States unless regulated by the States. As such, every state has gambling statutes to determine the type and amount of legal gambling permitted. With the development of the Internet, however, prohibitions and regulations governing gambling have been turned on their head. No longer do people have to leave the comfort of their homes and make the affirmative decision to travel to a casino—they can access the casino from their living rooms with the click of a button.

Since 1868, the federal government has enacted federal gambling statutes when a particular type of gambling activity has escaped the ability of states to regulate it. For over one hundred years, Congress has acted to assist states in enforcing their respective policies on gambling when developments in technology of an interstate nature, such as the Internet, have compromised the effectiveness of state gambling laws.

The negative consequences of online gambling can be as detrimental to the families and communities of addictive gamblers as if a bricks-and-mortar casino was built right next door. Online gambling can result in addiction, bankruptcy, divorce, crime, and moral decline just as with traditional forms of gambling, the costs of which must ultimately be borne by society.

Gambling on the Internet is especially enticing to minors, pathological gamblers, and criminals. There are currently no mechanisms in place to prevent youths—who make up the largest percentage of Internet users—from using their parents' credit card numbers to register and set up accounts for use at Internet gambling sites. In addition, pathological gamblers may become easily addicted to online gambling because of the Internet's easy access, anonymity and instant results. Dr. Howard J. Shaffer, director of addiction studies at Harvard, likens the Internet to new delivery forms of addictive drugs: "As smoking crack cocaine changed the cocaine experience, I think electronics is going to change the way gambling is experienced." Finally, Internet gambling can provide a nearly undetectable harbor for criminal enterprises. The anonymity associated with the Internet makes online gambling more susceptible to organized crime and money laundering.

I have long been a champion of the Internet and an advocate of limited government regulation of this new medium. However, that does not mean that the Internet should be a regulatory free zone or that our existing laws should not apply to the Internet. I think we can all agree that it would be very bad public policy to allow offline activity deemed criminal by states to be freely committed online and to go unpunished simply because we are reluctant to apply our laws to the Internet.

Gambling on the Internet has become an extremely lucrative business. Numerous studies have charted the explosive growth of this industry, both by the increases in gambling websites available, and via industry revenues. The Internet gambling industry's revenues grew from \$445 million in 1997 to an estimated \$4.2 billion in 2003. It has been reported that there are currently more than 1,800 gambling sites. Furthermore, industry analysts estimate that Internet gambling could soon easily become a \$10 billion a year industry.

Most of the more than 1,800 Internet gambling websites are operated from offshore locations. Virtual betting parlors accepting bets from individuals in the United States have attempted to avoid the application of United States law by locating themselves offshore and out of our jurisdictional reach. These offshore, fly-by-night

Internet gambling operators are unlicensed, untaxed and unregulated and are sucking billions of dollars out of the United States. In addition, the FBI and the Department of Justice have recently testified that Internet gambling serves as a vehicle for money laundering and can be exploited by terrorists to launder money.

H.R. 21, the Unlawful Internet Gambling Funding Prohibition Act will add a new provision to the law that would prohibit a gambling business from accepting certain forms of non-cash payment, including credit cards and electronic funds transfers, for the transmission of illegal bets and wagers. The bill also gives Federal and State law enforcement new injunctive authority to prevent and restrain violations of the law.

H.R. 21 will return control to the states by protecting the right of citizens in each State to decide through their State legislatures if they want to allow gambling within their borders and not have that right taken away by offshore, fly-by-night operators.

The 104th Congress created the National Gambling Impact Study Commission and charged it with conducting a comprehensive legal and factual study of gambling, including an assessment of the interstate and international effects of gambling by electronic means, including the use of interactive technologies and the Internet. The Commission recommended to Congress that federal legislation is needed to halt the expansion of Internet gambling.

As the National Gambling Impact Study Commission has documented, and Senate and House hearings have confirmed, Internet gambling is growing at an explosive rate. It evades existing anti-gambling laws, endangers children in the home, promotes compulsive gambling among adults, preys on the poor, and facilitates fraud. H.R. 21 will help to stop this harmful activity before it spreads further. I urge my colleagues to support this very important legislation.

HR 1223, the Internet Gambling Licensing and Regulation Commission Act, attempts to attack the Internet gambling problem from another angle, namely regulation. The bill establishes a commission to study the issues involved with the licensing and regulation of Internet gambling activities.

However, there are many concerns associated with setting up a national commission to regulate the offshore Internet gambling industry. Regulation would legitimize gambling activities, which have been shown to cause addictive behavior, bankruptcies, and associated family problems. In addition, it is doubtful that regulation would effectively curb the fraud, money laundering and other organized criminal activities associated with offshore Internet gambling websites.

Thank you again, Mr. Chairman, for holding this important hearing.

**QUESTIONS FOR WRITTEN SUBMISSION ON BEHALF OF
CONGRESSMAN BOB GOODLATTE
AT THE
CRIME, TERRORISM, AND HOMELAND SECURITY
SUBCOMMITTEE HEARING ON
HR 21 AND HR 1223
APRIL 29, 2003**

**QUESTION FOR JOHN G. MALCOLM,
DEPUTY ASSISTANT ATTORNEY GENERAL,
CRIMINAL DIVISION, U.S. DEPARTMENT OF JUSTICE**

As you know, I have sponsored legislation in the past to prohibit online gambling and to give law enforcement the necessary tools to aggressively prosecute those that violate our gambling laws. I believe that HR 21 goes a long way in combating the problem of online gambling and I am a proud co-sponsor of that bill.

As you know, last November, the 5th Circuit Court of Appeals ruled that the Wire Act, passed in 1961, applies to sports-related Internet gambling and not to other forms of gambling, such as casino-style gambling. Does the DOJ believe that this is the correct interpretation of the Wire Act? Is the prevention of other forms of on-line gambling a priority for the DOJ? What additional tools does the DOJ need to combat both sports-related and other types of on-line gambling?

**QUESTION FOR WILLIAM HORNBuckle,
PRESIDENT AND COO, MGM MIRAGE ONLINE**

The problems with traditional gambling are many. Addictions, bankruptcy and the troubles they bring to American families top the list. When gambling is made available to every online household in the United States with the click of a button, the problems listed above could become nationwide epidemics. Furthermore, Internet gambling introduces new concerns, such as the increased potential for (1) fraud and (2) gambling by minors at home.

Mr. Hornbuckle, do you believe that a regulatory scheme will ever curb all of the fraud and uncertainty that offshore gambling entities present to United States citizens? Even if you do believe that regulating these rogue entities is possible from inside the United States, how would regulation prevent the problems of underage gambling, bankruptcies and addictions that gambling already presents and that the rollout of Internet gambling threatens to make worse?



May 5, 2003

The Honorable Robert W. Goodlatte
 United States House of Representatives
 2240 Rayburn House Office Building
 Washington, DC 20515

Dear Congressman Goodlatte:

Thank you for asking me to respond to your questions on H.R. 21 and Internet gaming. Unfortunately, I find your initial statement and subsequent questions based on unfounded and inaccurate predicates.

In your initial statement, you claim "When gambling is made available to every online household in the United States with the click of a button, the problems listed above become nationwide epidemics." I would strongly suggest to you, as I did in my testimony that when is now! Today over 110 million American homes can access an Internet casino with the click of a button. H.R. 21 will do nothing to stop Internet gaming in the United States.

As for the negative impacts you alleged, research conducted in 1999 for the National Gaming Impact Study Commission found that the presence of casinos does not correspond to increases in crime or bankruptcy; a separate U.S. Treasury Study also found no bankruptcy link. Additionally, Commission research estimated that the pathological gambling prevalence rate was 0.6 percent in 1999, whereas in 1976 it was 0.77 percent. Despite a significant increase in gambling opportunities throughout the country, the rate has remained static, moving slightly downward.

We would respectfully remind you that prohibition in the United States has had a long list of failures associated with it. Unless the Committee is to propose unpractical, unenforceable, and draconian measures that would have far reaching impacts on e-commerce in general, prohibiting activity on the Internet, gaming or otherwise, will unfortunately suffer a similar fate.

Recently the British government, through the Department of Culture, Media & Sport, issued a position paper on the future regulation of remote gambling (see attached). The Government took the position, "that continued prohibition was neither desirable nor practical. All of the evidence pointed towards a growing global market for online gambling where national boundaries had come to little meaning. Nowhere is this better illustrated than in the United States where, despite the apparent illegality of cross border gambling, more of its citizens gamble online than anywhere else in the world. To deny this appears in many ways to fly in the face of the reality of international banking and the inherently international nature of 21st Century telecommunications."

The Honorable Robert W. "Bob" Goodlatte
May 5, 2003

Since the British government has clearly taken a position of support for proper and effective regulations of online gaming and has also adopted a position of no "blacklist of countries from where to accept customers," I would suggest that any modicum of control H.R. 21 is looking to impose on U.S. citizens would further slip away under the proposed United Kingdom regulatory environment. It takes under one second to reach a server in the United Kingdom.

Although we do not subscribe to your specific beliefs on addictive and underage gambling or the concerns that others have raised with respect to money laundering, I do not understand how H.R. 21 cures or deals with any of these important issues. You raised the question, "Do you believe that a regulatory scheme will ever curb all of the fraud and uncertainty that offshore gambling entities present to United States citizens?" I would ask you and your fellow Committee members to consider the following counter-question: How can we not regulate and control a product that cannot be reasonably stopped, particularly in view of the fact that, unlike in 1999 when the National Gambling and Impact Study Commission advocated against Internet gaming, tools and regulations exist today to provide a very high level of reasonable assurances that jurisdictional restraints, problem gambling, underage gambling, and money laundering can be controlled?

We urge you again to consider the merits of H.R. 1223, which call for an Internet Gambling Licensing and Regulatory Study Commission. Only through research and study can sound and effective legislation be drafted, passed, and enforced. The American public, in ever increasing numbers, clearly enjoys this activity. They deserve the protections that only proper regulations can provide.

It can be done. It should be done.

I ask you, Congressman Goodlatte, if H.R. 21 is passed, what will stop my fourteen-year-old daughter from gambling online the very same day this bill is enacted, without the controls that can only be found in properly regulated environments?

Respectfully,



William J. Hornbuckle
President & Chief Operating Officer

Attachment: Department of Culture, Media & Sport Position Paper:
The Future Regulation of Remote Gambling

cc:

THE FUTURE REGULATION OF REMOTE GAMBLING: A DCMS POSITION PAPER

Department for Culture, Media & Sport
April 2003

**THE FUTURE REGULATION OF REMOTE GAMBLING: A DCMS
DISCUSSION PAPER****Contents**

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Introduction

Gambling Review report and the Government's response

The Gambling Review report was published in July 2001. One of its major recommendations was that online gaming should be permitted in the UK (the related commentary and recommendations are to be found between paragraphs 30.20 and 30.43 of the Review Body's report). That recommendation was endorsed in the Government's subsequent paper '*A safe bet for success*' which was published in March 2002. Both documents can be found on the DCMS website at www.culture.gov.uk.

2. Although both pieces of work supported the principle of a properly regulated UK based online gambling industry, neither of them was the right vehicle to consider the issues in detail. Since they were produced further consideration has been given to the practical implementation of this policy.

Next Steps

3. The necessary legislation will be contained in the Gambling Bill that is currently being drafted. The Government's intention is that the draft Bill should be the subject of a full pre-legislative consultation process. This will include both a public consultation exercise and a scrutiny of the Bill by a Parliamentary Committee. However, the Bill will only provide a regulatory framework and, as this is an area of gambling regulation that is largely new, it has been decided to take this opportunity to make publicly available its current thinking on some of the major issues in this field.

4. Consequently, the purpose of this paper is to outline how best the Government might achieve its aim of introducing a reliable system of regulation for a newly legalised onshore remote gaming industry. It will also seek to show how the existing remote betting operations could be incorporated within the same regulatory framework.

5. Many of the issues associated with remote gambling are interlinked, but for the sake of clarity this paper seeks to break them down under a number of key headings. They are:

- Background
- Role of the Gambling Commission
- Licensing
- Player Protection
- Safeguards for the young and vulnerable
- Player identification and verification standards
- Money laundering & payment methods
- Systems and software
- Territoriality
- Taxation

- Advertising
- Remote gambling in non-licensed public premises

6. Due to the rapidity of technological developments this, perhaps more than any other, is a sector of the gambling industry where flexible, responsive regulation will be a necessity. This can only be achieved by ensuring that the relevant parts of the legislation are broadly framed in certain areas. It follows that much of the detailed regulatory measures and procedures will be left to the Gambling Commission to determine.

7. Before implementation of the legislative reforms it will be important for DCMS and the Gambling Commission, when it is established, to maintain a constructive dialogue with interested parties, especially those within the gambling industry. It is only right that everyone involved seeks to keep an open mind about these issues and if the proposed regulatory controls envisaged in this paper prove to be unnecessary or, more probably, if the regulatory objectives can be achieved in better ways then they can still be amended. This paper then is, as its name implies, a snapshot of the Government's views. Those views have been shaped over a period of time and with a great deal of deliberation. The headline policies are very unlikely to change, but few of the details are set in stone. The main planks of Government policy for remote gambling can be adapted as necessary by the Gambling Commission so that they are appropriate to the activity in question.

Background

8. If there is one quote from '*A safe bet for success*' that sums up the Government's approach it is perhaps the following:

'Licensing and regulating online gambling will present a number of challenges that do not necessarily arise through more traditional forms of gambling media. The Government is satisfied that these challenges can be met, not least by giving the Gambling Commission sufficient flexibility to respond promptly to any new technological advances that may undermine the regulatory regime.' (Para 4.50)

9. That statement sets the boundaries for both this paper and any ensuing discussion of the issues. There is an obvious need to address the issues from a policy perspective and in the following pages there are suggested methods for meeting the 'number of challenges' that exist, but they can and should only go so far. At the end of the day the detail of the licensing and regulation of online gambling operators must be for the Gambling Commission. There is no alternative if it is to have the sort of 'sufficient flexibility' that it needs in moving forward.

10. The Gambling Commission will have broad powers in relation to the regulation of remote gambling. In spite of that it does not seem unreasonable in certain areas to give examples of the type of steps that the Government might expect the Gambling Commission to take in discharging its regulatory functions if these freedoms can be acquired.

Definitions

11. During most of the policy development phase the term 'online gambling' has been adopted as a catch-all phrase. It was used in both of the publications mentioned above. Others such as I-gambling, E-gambling or wireless gambling could have done just as well. In the legislation and in this paper the term 'remote gambling' will instead be used. The reason for this is that the Government wants the regulations to be technology neutral and to cater for all forms of player-not-present gambling. What matters is that there is a common understanding that the delivery systems included in these definitions encompass the internet, interactive television, and any other remote access devices that are currently available and, just as importantly, might be developed in the future.
12. For reasons which are readily apparent not every measure applied to one form of remote gambling will be precisely transferable to another (for example, the much smaller screens of VAP and next generation phones will impose different physical constraints on the links that might be made available at all times on them). That does not mean that the same regulatory principles cannot be applied to them.
13. It is envisaged that their starting point will be the regulation of online (eg internet or interactive) gambling which can then be tailored to meet the demands of other delivery systems such as the telephone. In the light of this most of the discussion in this paper focuses on online gambling.

The existing online industry

14. By its very nature the remote gambling market is a global one. This makes it very difficult to be precise in any way about its origins, size or potential. But to put matters into perspective it is worth quoting some indicative information:
- The first sites seem to have appeared in the mid 1990s.
 - It is estimated that there are already around 1700 sites (indications are that increased consolidation might mitigate against a significant increase in this number).
 - A Datamonitor 2001 report concludes that by 2005 there will be 15 million online gamblers generating a turnover of \$30 billion (other estimates vary but all underline that this is a significant and growing international market).
 - Over 50 jurisdictions already allow some form of remote gaming.

The Government's approach

15. This means that for both operators wishing to be based in Britain and for the Government itself there are already many lessons, good and bad, to be learned from what has already happened in other jurisdictions. While the

basics of good gambling business management and good regulation hold true no matter what the environment it has to be accepted that there are aspects of remote gambling that are unique. A slavish adherence to what might or might not have worked in bricks and mortar establishments in the past is neither appropriate nor sufficient.

16. The Government has shown itself to be mindful of the commercial imperatives that will determine whether operators will choose to be based here in the future and Ministers have expressed a hope that Britain will come to be a world leader in all fields of gambling activity. If the Government is going to create the right conditions for operators to thrive it will expect operators to adopt a co-operative approach. Ideally this will manifest itself in a shared commitment to the principles of good regulation, but as a minimum it must expect compliance with licence conditions and the adoption of socially responsible practices.

17. Remote gambling, by any criteria, has to be placed at the harder end of the gambling spectrum. That brings with it responsibilities for both operators and regulators. It must entail proportionate regulatory measures, but this does not have to mean over-regulation for the industry. Proper regulation should be welcomed by operators and in the main this seems to have been recognised. It will improve the credibility of the industry as a whole and should serve to reinforce the brands of operators licensed in this country. Customers have a right to expect probity and fairness. That must be deliverable.

18. Interests will rarely coincide precisely, but there is no reason why a suitably regulated remote gambling industry should not be of real benefit to the Government, operators and gamblers alike. This shared goal represents a very firm basis on which to build.

Role of the Gambling Commission

Skills base

19. The staffing structure of the new Gambling Commission has yet to be determined. Irrespective of its final organisation and form it will need to acquire the expertise to develop and maintain a detailed regulatory licensing framework for remote gambling. This must include the ability to satisfy itself as to the quality of the systems being used.

20. There are a number of reputable companies that provide software and systems testing services. It is not necessary for the Commission to take on this function directly and it should have the power to authorise a number of these companies to undertake that role. This would negate the need for the Commission to employ a large number of IT specialists. Nevertheless it is vital that the Commission has adequate resources in this area to monitor the performance of its 'sub-contractors' and to provide independent and expert advice to the Commission on related policy areas. Fortunately several

members of the Gaming Board's staff (who will provide the nucleus of the new Gambling Commission) have already shown themselves to have a good grasp of both the policy issues and the practicalities of this type of regulation in the future.

Powers

21. As with other sectors the expectation is that codes of practice will be issued by the Commission to licensed operators and these will be used to inform any decisions about whether or not they are abiding by the conditions on their licences. The codes will also set out the parameters within which operators can manage their businesses. It is intended that this will give operators sufficient leeway to develop and introduce new products without continual reference to the Gambling Commission.

22. The ability to issue or revise these codes will equip the Commission to respond quickly and effectively to new developments, technical or otherwise.

23. Although remote gambling is non-premises based, the Commission will need access to some of the operators' hardware and software (for example, primary gaming servers) and their inspectors will be given powers of entry, search and seizure.

24. Full details of the Commission's powers and sanctions will appear in the draft Bill to be published later in 2003.

Kitemark

25. It will provide a kitemark that, wherever possible, licensed operators must display on their sites. As a minimum that should appear on any internet home pages. It would be helpful if that kitemark could also double as a hotlink to the Commission's own website where, amongst other things, there would be an easily accessible register of all licensed operators. This would offer immediate reassurance to players wishing to try a site they were unfamiliar with and, hopefully, will go some way to prevent the possible pirating of the Commission kitemark.

Licensing

Operator and personal licensing

26. Levels of licensing across the whole gambling industry are under review separately, but all licensed operators will have to go through a thorough process to check their probity, their financial resources, and their expertise. As a minimum there will still be both operator and personal licensing.

27. For remote gambling the former of these speaks for itself. However, different types of remote operation will require different levels of finance and different types of expertise. Essentially there will be three categories of

remote licence, one for gaming, one for betting, and one for lotteries. Below that the Gambling Commission will adopt a pragmatic approach applying different tests, for instance, to an operator who only wants to run an online betting exchange as a betting intermediary, to those applied to a bookmaker merely wishing to run a telephone betting operation.

28. Obviously someone already holding a betting operating licence will not, in practice, have to go through the whole process as he will already have passed a comparable probity check and the focus would only be on the operation of the remote betting. A great deal of thought was given as to whether betting operators should automatically be allowed to offer remote betting without an additional licence. It was concluded that the checks would have to be made irrespective of which licence category remote betting fell in to and that in the interests of consistency remote gambling should be licensed in the same way as remote gaming. This was even allowing for the fact that remote betting raises less concerns than remote gaming because betting operators are not in control of the gambling event itself. Therefore, there are less fair play and player protection issues to address. Pulling in the opposite direction was the fact that there is a much greater similarity between remote betting and gaming when it comes to the other core regulatory objectives of combating criminality, protecting the vulnerable, and preventing underage access. Naturally just because, for instance, a company holds a betting operating licence it does not mean it will automatically qualify for a remote licence, but the aim should be to avoid any duplication of checks already made and to streamline the process as much as possible.

29. The level of personal licensing is more problematic. Below the licensed operator (be that an individual or the more common corporate body) there is a strong case for, as a minimum, having a personally licensed compliance officer. Apart from that, this is one of the detailed areas that would benefit from further discussion between the industry, Government and the Commission. It is likely though that the Gambling Commission will specify posts that have certain characteristics.

Licence costs

30. The price of any gambling licence should as far as possible be set at a level that meets not only the cost of issuing the licence but also the associated regulatory cost of monitoring that activity on the basis that this is a service to applicants. Licences will be time limited. The Bill will set out the details but the proposal will be for operating licences to run for ten years.

31. Until a detailed costing exercise is conducted there is nothing to be gained from speculating about the future price of an online operator's licence. But, solely for illustrative purposes, it is worth noting that in Antigua (where there are 90 or so sites) an online casino licence costs \$100,000pa and an online sports book licence is \$75,000pa; and in Alderney a three year online gaming licence costs £75,000.

Licence conditions

32. Although the Gambling Commission will be empowered to issue its own codes of practice it is likely that it will need to attach particular licence conditions over and above standard requirements to any of the licensed online operators. This should not raise concerns amongst potential licence holders, but if it does then they can take reassurance from the fact that a robust appeals system is being developed so that there will be a formal, independent process for reviewing decisions made by the Commission.

Player Protection

Informed adult choice

33. One of the core elements of good gambling regulation is player protection. That applies as much to remote gambling as elsewhere. Indeed, given the relative lack of transparency of remote gambling operations, it is must be even more of a precondition.

34. An underlying principle of the planned gambling reforms is informed adult choice. In online gambling for instance that means that information is made available to the player and the information must be as accurate as possible. That includes rules of play, game representation, and rates of return.

35. Behind the scenes where the player cannot have access to systems it is the responsibility of the operator and the regulator to ensure that the gambling event (primarily the random number generator) and all the procedures linked to it are fair and reliable. The section on systems and software covers this in more detail.

Practical measures

36. In the final instance the core needs of an online gambler are fairly few. It is not a definitive list, but those frequently stated are fair games, entertainment, simple procedures, fast payment methods, privacy and security. How successfully some of these are provided will be a purely commercial decision for the operator. Others will need input from the Gambling Commission.

37. Many protection measures will be covered in later sections on identification and payment methods. Aside from those the Gambling Commission will wish to include in its codes instructions on the following:

- Privacy – safeguards to ensure that personal information provided to gambling operators is secure and used only for the purposes that it has been supplied (compliance with the Data Protection Act will be mandatory).
- Security – the provision of reliable systems to ensure that financial transactions are as secure as possible.

- Customer service – availability of clear dispute resolution procedures, customer helplines & operator e mail addresses.
- Information in other languages – if an operator is going to advertise and, or, accept bets in foreign languages then social responsibility information should be made available in those languages too. In other words the same player protection safeguards should be in place.

Safeguards for the young and vulnerable

Underlying importance of the issues

38. Preventing underage gambling and combating problem gambling have always been at the heart of the Government's regulatory objectives. The extent to which the Government opens up the gambling market will largely be determined by how confident it can be that these objectives will not be undermined.

39. For various reasons more questions may be asked of the new online gaming sector than any other part of the gambling industry. It is untested, it lacks many of the physical controls available to premises based gambling, it facilitates unsupervised gambling, and it will be more widely available than any other gambling product. This underlines why the Government attaches so much importance to regulating it effectively.

40. Detailed measures will be for the Gambling Commission to finalise in co-ordination with operators and experts in the field, but this aspect of online gambling is one on which the public and Parliament will want some real assurance that the risks can be properly managed. While there can be no absolute guarantees, it will be essential to put in place a package of viable measures that will minimise the downside of any reforms.

Practical safeguards

41. Online gambling is still a relatively new phenomenon and reliable research about its effects is at a premium. Once more becomes known about this field the Gambling Commission will be well positioned to respond. Such an evolutionary approach should produce an increasingly focussed and well-informed body of practical safeguards to address every potential area of problem gambling.

42. As with the other gambling sectors this will call for ongoing liaison with the industry and those organisations, such as Gamcare and Childnet International, that specialise respectively in the treatment of problem gambling and the overall problem of child access to unsuitable sites.

43. In the meantime it is not unreasonable for the Government to indicate the sort of controls it would expect and to offer some specific examples for the

Gambling Commission to consider. For ease of reference they are grouped together in several categories:

Screening of players

- More detailed consideration of this subject is in the next section on identification and verification standards, but it cannot be stressed too frequently how important this is in preventing children from gaining access to gambling sites.
- At every stage of the registration process there should be clear and persuasive warnings that children are not allowed to play and that if they are discovered to be doing so any deposited funds may be forfeited. A warning that comprehensive checks will be made to verify information given should also act as a deterrent.
- The only exception to this will be in those very few areas (eg football pools and lotteries) where the current age limit is 16 rather than 18. This will call for careful handling, but could be accommodated.

Reality checks

- As it is the escape from reality that underpins so much of the problem gambling that exists, adequate reality checks must be available.
- Most of these checks will be voluntary in nature. Players must have the opportunity to self limit their losses, the amount of time they play for and even to exclude themselves from the site for whatever period they determine. If any of these limits are passed then the operator must exclude the player until the prescribed period has passed.
- There are also attractions to having counters on display that automatically update a player's balance.
- Above these checks it is recommended that there is an automatic reality check imposed on the player at least every hour. This need not be onerous for operator or player. It should be sufficient for play to be suspended; for a message to be displayed telling the player how long they had been playing for and how much they were winning or losing; and for the player to click once to confirm he had read the message, and for him to then be given the option of ending the session or returning to the game. This procedure would take only a few seconds but would require the player to stop and, in the light of time and cost, make a rational decision about whether to continue or not.

- Having a clock continuously on screen could be useful, but some reservations have been expressed about refresh rates and their accuracy. If problem gambling experts feel this is worth pursuing then the Gambling Commission could revisit this option, but the combination of a compulsory break after an hour and a prohibition on anything that obscures a PC's own clock could be sufficient.
- Player perception is always a factor to be considered and there is a risk that they can lose their appreciation of the real value of money. Together the measures mentioned here will go a long way to preventing difficulties, but it would also be worth insisting that all amounts quoted are given with the symbol of the currency that the player is using. It is not unknown for existing sites to merely show a figure (eg 10, 50 or 100 rather than £10, £50, £100 – this is not helpful to the problem gambler). This would not call for the site to display a wide range of different currencies but rather to continue to display the symbol for whichever currency the player is playing with. For example if the player was depositing US dollars and the operator exchanged that for British pounds then the counter would only need to show the player's running total in pounds and not in dollars.

Responsible management

- Staff should be trained to identify any gambling patterns that may indicate that the player has a problem and to be aware of wider social responsibility issues.
- In developing or upgrading games or types of bet the operator should bear in mind any social responsibility guidance or codes issued by the Commission.
- Players should have ready access to their playing history (ideally no more than two clicks from the home page) so that they can easily monitor their long term performance and have the information available to make an informed choice about whether to continue and how much to risk.
- The ability of operators to offer credit or inducements to gamble carry with them a heavy responsibility. They are both cross-cutting issues of particular sensitivity and ones which will be considered further. These sorts of business developments are common place in other parts of the leisure sector and used responsibly are valid marketing tools. Despite that it has to be recognised that gambling as an activity is perceived differently to many other types of leisure activity and, as noted elsewhere, can carry with it a risk of harm. The Gambling Commission will not want to restrict the commercial freedom of operators, but it is

inevitable that it will want to monitor operators' practises particularly carefully.

Filtering services

- It would be good practice for all gambling operators to register with a filtering service such as Internet Content Ratings Association (ICRA), NetNanny or Safesurf. ICRA, for example, provides software to parents who can then use this free service to prevent children being able to visit gambling websites.

Play for fun games

- Many operators will wish to offer free play versions of their games. There is nothing wrong with this in itself and it may well be an effective marketing technique. These games cannot be allowed to offer a misleading impression of the real games; playability and rates of return must be the same in both cases.
- If there is an issue around free to play games it is whether or not they are accessible by children. The concern is that if they are it will arouse their interest, possibly contribute to problem gambling at a later date, and may encourage them to evade controls and play on the real games. It can be argued that gaming simulation software is already popular and readily available and there are no restrictions on its sale to children. Further consideration needs to be given to this issue.

Payment methods

- Gambling operators will be able to accept a wide range of payment methods. Some of these, such as credit cards, are usually only available to adults. It is therefore anticipated that when inspecting an operator's business the Gambling commission will look closely at those transactions where payment is from a source that might be available to children. An example would be the Solo debit card.
- The Gambling Commission would also have the option of pursuing with banks and the Financial Services Authority whether it might be possible to build in a new age identifier to credit and debit card numbers to assist operators in filtering out underage players.
- Banks are understandably protective of data relating to their clients. This should not prevent them from co-operating with gambling operators if there is any margin for them to do so. Even if they cannot provide information, it would be an enormous help if they could confirm any details put before them

by licensed gambling operators. This is another area where the Gambling Commission may be able to play a productive role.

Displays

- Operators should be prevented from offering full screen games on computers (this would ensure that the PC's internal clock is visible at all times).
- Links to the Gambling Commission and information about problem gambling should be available on screen at all times. The latter should include advice about underage play, symptoms of problem gambling, details of player protection (such as reality checks) options on the site, and details of where a player might be able to turn to for support if required (eg Gamcare, Gamblers' Anonymous etc).

Rapidity of play

- Rapidity of play is a well known driver of gambling addiction and the Commission should make best use of any research that emerges in this area to ensure that, if necessary, proportionate restrictions can be put in place.

Parental responsibility

44. In opening up the remote gambling market the Government and the Gambling Commission can be expected to do everything in their power to prevent children from gaining access to gambling sites. But there are also additional steps that responsible parents can take.

45. With the proliferation of delivery systems, especially home computers and interactive television, personal supervision has become increasingly difficult. Despite this parents must bear some responsibility for the material that their children access. Registering with filtering services will be one weapon at their disposal. The Gambling Commission will inevitably play a part in the Government's push to raise the awareness of parents in this and other areas of potential risk (see following section).

Related internet initiatives

46. Both law enforcement agencies and parents have voiced concerns about some of the sites and services to which children can gain access. It is fair to say that gambling sites have not figured prominently amongst these concerns, but some of the initiatives may well pay dividends in this area anyway.

47. The Gambling Commission will have to cast its net wide to keep abreast of developments. Current examples of the sort of initiatives it might be able to call upon are outlined below:

- The present Communications Bill will give a new regulator, OFCOM, the task of promoting 'media literacy' so that people will be in a better position to make informed decisions about what they and their children access;
- The EC's 'Safer internet action plan' has provided a budget to (i) promote hotlines to report illegal content; (ii) develop filtering and rating systems; and (iii) promote awareness of internet dangers and how to protect children from undesirable content; and
- The Home Office's Internet Task Force is considering how to improve the protection of children from inappropriate content of all kinds.
- The new Interactive Age Check service operated by Citizencard (www.citizencard.net) allows operators to verify user details against existing proof-of-age databases.

Underage gambling - final responsibility

48. The Gambling Commission will of course do all it can to enforce best practice to prevent children gambling, but it cannot be emphasised strongly enough that the ultimate responsibility rests with the licensed gambling operator.

Player identification & verification standards

49. It is in the interests of the players, the operators and the wider public good that there should be high standards of identification and verification. They are crucial to combat crime, fraud, and underage play.

50. In what will be a truly international market there can be no one size fits all model of what identification evidence is required before a player can open an account. It will therefore fall to the Gambling Commission to set minimum standards, probably which reflect personal data that is available in this country. Above this operators would be expected to use the best publicly available information for verification purposes from whichever country the player is situated in.

Registration process

51. The point at which a prospective player registers on a site is self evidently the first step in the process. There is fairly common ground over the most basic information that should be requested (name, address, e mail, phone number, age, bank details, preferred payment methods etc).

52. But it is the next step, when the operator must verify that this information is truthful, that is really vital.

Verification

53. No system of verification can be completely foolproof, but there are already various sources of information about people that can be readily accessed to help confirm that the person registering and opening an account is who he or she claims to be.

54. A number of commercial databases provide the sort of service that gambling operators will need to employ and they already help other industries in assessing the credit worthiness of their customers. Information can be drawn from these services electronically within seconds and their use should not deter players seeking to register with gambling operators in Britain.

55. It will be for the Gambling Commission to map what is available and on that basis to issue guidelines for operators to use, but there is nothing to be gained from being prescriptive about sources this far removed from the issuing of licences.

56. At the far end of the verification scale are systems such as the 'hundred point check' which calls for the supply of a very wide range of information, such as certified copies of passports and employer references, before an account can be opened. There can be little doubt that this level of verification would act as a disincentive to players interested in using British sites. More importantly, it would not be a proportionate level of regulation. It is suggested that a more pragmatic approach for any Gambling Commission guidance to use would be a risk-based layering model.

57. In broad terms the layers might be:

- a. Basic registration questions (anecdotal evidence indicates that even this filters out some underage players);
- b. Location checks (see section on IP addresses below);
- c. ID checks relating to name, date of birth & address;
- d. Banking checks (are the cards being registered valid, were they issued in the player's country of origin etc)
- e. Credit risk assessments.

58. At the end of even this basic process the operator will normally have enough information to determine whether or not to allow the player's registration to proceed. However, as the risk remains predominantly with the gambling operators, it would still be open to them to request written proof of

identity (a copy of a passport or ID card are the most commonly quoted types) if an unacceptable degree of doubt remained.

59. Like so much in the field of emerging technologies it is impossible to predict what the next helpful development might be. Things like the increased use of smart cards, e-signatures, or even finger or retina scans may aid the operators and regulators of the future. All they must do is remain open-minded and ready to make the best use of whatever becomes available.

60. Following these checks the player should be given a dedicated user name and password. These should provide a safeguard against someone else accessing the player's account. A further example of good practice would be to prevent the player from depositing or withdrawing funds above a set level unless they had a unique digital code to input. This code would only be available to them after it had been sent by mail to the address given when they registered. This would combat fraud, confirm the player's whereabouts, and may make it even more difficult for underage players to conceal themselves.

Internet Protocol (IP) addresses

61. IP addresses are frequently referred to as a useful device for identifying a computer user's whereabouts. They are by no means completely reliable, but they are usually accurate. They could help gambling operators confirm that a player is in the country he claims to be in (for verification purposes) they could also help the Gambling Commission to police any restrictions that may be placed on the jurisdictions from where players are gambling (see section on cross border gambling).

62. Either way, in order to put this into context, there is merit in briefly outlining what an IP address is and how the addresses are allocated.

63. The address itself is a unique numerical code allocated to every computer that can be used to access the internet. It identifies both networks and individual computers.

64. The addresses themselves originate from the Internet Assigned Number Authority (IANA) which allocates blocks of addresses to Regional Internet Registries (RIRs) which then assign them within the areas they are responsible for. The three RIRs cover the following geographical areas:

APNIC	-	Asia/Pacific
ARIN	-	Americas & sub-Saharan Africa
RIPE NCC	-	Europe & surrounding regions.

65. The RIRs can assign addresses in further blocks and there are different classes of address depending on usage.

66. These electronic addresses are exchanged whenever computers communicate over the internet. Filtering software or tracking services at the

gambling operator's end should be able to use the IP address to automatically check the location of the player.

67. More than one operator presently based offshore has praised the benefits of this system. If it is truly dependable then the use of a mechanism of this kind ought to be encouraged. However, before any over reliance is placed on it, the Gambling Commission will need to consult the IANA, the RIRs, and others to determine properly its worth and how easily the protections it appears to offer can be circumvented.

Money Laundering and payment methods

Money Laundering

Background

68. The issues surrounding domestic and international money laundering are complex and longstanding. This means that there is already a high level of experience within British law enforcement agencies, especially the National Criminal Intelligence Service (NCIS), for the Gambling Commission to refer to. As part of the gambling review process the DCMS established a Crime Issues Group where these agencies were represented. It provided a forum where detailed consideration could be given to these matters.

69. More widely multinational organisations such as the 31 member Financial Action Task Force (FATF) have been, and will continue to, take a close interest. Its 2001 paper, *'Report on Money Laundering Typologies'* indicated that in some of its members' states there was evidence that online gambling had been used as a way to launder money. However, no further information on this has become available and there appears to be a paucity of proof that this is a significant problem.

70. Using this available expertise and taking full account of initiatives such as the EC Money Laundering Directives, the Gambling Commission would be expected to play a full part in combating money laundering.

71. Underpinning all this would be a requirement for operators to comply with any present and future Money Laundering Regulations issued by the Government. The Gambling Commission is likely to issue its own advice to licensed operators on practical steps that might be taken to comply with those regulations.

Safeguards

72. It is safe to say that gambling transactions completed online can be more secure than cash business conducted in traditional gambling outlets. There can be no room for complacency, but the presence of audit trails, registration processes, and the fact that operators will have a double due diligence system in place (eg having not only their own anti-money laundering

procedures in place but also those of the existing banking system when taking and paying out funds. This will offer a good degree of reassurance.

73. For the sake of completeness, one risk that must be mentioned is the possibility that a criminal organisation seeking to launder large amounts will actually try to obtain a remote gambling licence to run its own gambling business. This would make it much easier for the money laundering controls being placed on players to be avoided. But this is a risk in all areas of gambling and will be addressed by the Gambling Commission's vetting process when applications are made.

Payment Methods

Which methods?

74. Because it is the most popular, there is a tendency to assume that credit cards will continue to be the most common method of paying for remote gambling. This cannot be taken for granted, particularly as the global market expands further into regions where credit cards may be less available or less fraud resistant than is perhaps the case in Britain. There is also the possibility that, as in the USA, credit card companies may no longer allow their services to be used to facilitate gambling.

75. Nor can one say with any certainty what the next best option may be, since all are at risk from possible restrictions. For example, in August 2002, PayPal, the electronic payment service, agreed to block online gambling operators from using its transaction system to process payments from players based in New York State. This followed an enquiry by the New York Attorney General.

76. Consequently, there should be no restriction (except perhaps relating to money laundering concerns) on operators accepting other payment methods that could include debit cards, cheques, wire transfers, cash deposits, pre-pay, smart cards, third parties (eg paybox) etc. If this is the case then Gambling Commission controls would have to relate to the risk of each, with credit cards being at the safer end of the spectrum and cash deposits at the opposite end. If suitable controls cannot be identified for a particular payment method then the Gambling Commission would not approve its use.

77. The Gambling Review Report (para 30.33) recommended that payments should only be made back on to the cards or accounts from which deposits had originally been lodged. Although it did not explicitly refer to other types of payment method, this principle holds good for most of them. Cash deposits are the clear exception, but these are likely to be unattractive to most operators and should be rare. Where they are used then money laundering controls must be imposed which are at least as strict as those currently applied to cash gambling in a bricks and mortar casino.

78. Where these payment methods are available to children it will be the operators' risk if they choose to accept them and it is to be expected that when carrying out inspections the Gambling Commission may look more closely at those sorts of accounts.

79. A detailed issue that has been raised is whether or not players should be allowed to use more than one payment method or to register more than one type of card as a source of gambling funds. At present it is not clear that this would have any significant practical effect in preventing problem gambling as, even if it was imposed, players would have the option of simply changing sites/operators and carrying on regardless. If anything, this is a good example of a specific topic where better research on player behaviour is needed before the Gambling Commission acts to add a restriction on the industry.

Account management

80. As part of the procedure for obtaining a remote gambling licence the operator will have to demonstrate the security and efficacy of the financial systems it will employ.

81. It is accepted good practice that funds in players' accounts are held separately and are recoverable by the players even if the operator encounters financial difficulties. The failure of a number of online bookmaking companies in recent years underline the dangers if this is not made compulsory. It follows that this ought to become an explicit condition and one that Gambling Commission inspectors monitor as a matter of course.

82. There can be little justification for a player having more than one account with a particular operator and, given money laundering concerns, this should not be allowed.

83. Gambling on credit is a pan gambling industry issue where an overview will be taken. The only observation made here is that betting on credit is traditionally popular, has raised relatively few problems and, if removed, would have serious implications for the bookmaking industry.

Systems & software

Systems' approval

84. The Interactive Gambling, Gaming & Betting Association (IGGBA) has proposed that the Gambling Commission should approve operational systems, equipment and processes, and technical competence. It is accepted that this would provide the comprehensive level of regulation that the Government would want to see.

85. Precisely what should be tested under each of those headings will demand further discussion. However, it is anticipated that it would include:

- The operation of the Random Number Generators (RNGs)
- IT report systems;
- Security systems (eg UK banks use a 128 bit encryption system and gambling operators should do likewise);
- Backup systems;
- Disaster recovery systems;
- Account systems;
- Player protection measures;
- Banking facilities;
- Contracts with third parties;
- General compliance and internal controls (eg limiting staff access to critical systems); and
- Software compliance (including game specifics, presentation etc).

Servers

86. Servers are the mechanisms that hold all of the information relating to the gambling operation and, for gaming, where the virtual result and its presentation are generated.

87. The main issues relating to servers are their location and access to them by the Gambling Commission.

88. There is no need to be overly restrictive in this regard and there may be good commercial reasons why gambling companies will wish to put part of their operation on servers located overseas. It would though be unacceptable if this included the gaming itself and critical records (eg the RNG, game logic, player/game/financial records, audits, reports and casino management software) and these must be held on a primary server based in the UK so that Gambling Commission inspectors have not just online but also physical access to them.

89. The Gambling Commission will have to draw a clear line between what must be on the primary server mentioned above and any secondary servers (that could be based in the UK or elsewhere) which could perhaps be permitted to hold items such as graphics, website material, download software, and archived records.

Random Number Generators

90. RNGs are algorithm driven systems that produce the result of online games. In reality it is the generation of these numbers that is the gaming event on which people wager. They are at the core of every online gaming product and it is essential that the Gambling Commission can be assured that they are run honestly, reliably, and within certain parameters.

91. There are many tried and tested RNGs available, but the Gambling Commission will still need to satisfy itself about them and any new versions

that arrive on the scene. This will require both initial approval and ongoing testing once they are in use.

Games

92. It is explicit in the systems approval process outlined above that various aspects of gaming software will also have to be approved before they can be used.

93. A distinction has to be made between the software driving the game (and producing the result) and how that game is presented to the consumer. At the most basic level all online games are RNG produced irrespective of whether they look like roulette, slot machines or anything else.

94. If the RNG has been approved and the presentation of games is covered by Gambling Commission guidelines, there will be no need for the operator to obtain Commission approval before introducing a new game or presenting an existing game in a new way. This will reduce the workload for the Gambling Commission and give operators the commercial freedom they need to refresh the front end presentation of games at a rate that will enable them to compete with offshore competitors.

95. For this to work to everyone's satisfaction there must be a balance between control, inhibiting change and the operator's ability to respond to market demand. Given a sensible approach on both sides this must be attainable.

96. A recent development, but one that may well continue to grow in popularity, is person to person or multiplayer gambling (such as online card rooms). On the face of it the regulation of mainstream remote gambling could easily be adapted to adequately cover this sort of gambling too. It does raise slightly different questions about player protection and money laundering, but suitable audit checks and monitoring should suffice to deal with them satisfactorily.

Testing of systems

97. IT testing will be needed both on entry when applying for a licence and afterwards. While the Gambling Commission will have its own experts in this area, it would be much more practical and cost effective to sub-contract the bulk of this work to companies specialising in providing accredited testing facilities. The Gambling Commission will need to determine how best to enlist the assistance of external bodies in testing systems prior to licensing.

98. The Gambling Commission will set out exactly what it requires of these companies and an operator would not be granted a licence until a certificate of approval has been supplied by one of them.

99. The testing companies could 'fingerprint' all code modules used to ensure that the software that was originally tested was that being used once

the gambling operation was up and running. Random remote testing should then be sufficient for monitoring purposes in nearly all cases. This is not to rule out other options that the Gambling Commission may wish to consider in the light of experience or new best practice.

Role of Service Providers

100. ISPs, telephone companies and similar service providers offer conduits for gambling operators and their customers to make contact and do business. They are not providers of the gambling product. Irrespective of whether any have responsibility for the content of the material provided through them, it is expected that they would co-operate with the Gambling Commission where appropriate.

Cross border gambling

101. The growth of this activity through remote means has put this issue firmly on the international agenda. The UK's prospective position on this has sparked a good deal of international interest from operators, regulators and governments. It is therefore important to explain the stance taken.

102. In taking the decision to accept the Gambling Review body's recommendation to allow British based online gaming, the Government took the view that continued prohibition was neither desirable nor practical. All of the evidence pointed towards a growing global market for online gambling where national boundaries had come to have little meaning. Nowhere is this better illustrated than in the USA where, despite the apparent illegality of cross border gambling, more of its citizens gamble online than anywhere else in the world (it is estimated that they still constitute over half of the online gaming market).

103. To deny this appears in many ways to fly in the face of the reality of international banking and the inherently international nature of 21st Century telecommunications.

104. This is not to say that the issues are by any means clear cut and full note was taken of other viewpoints such as that of the well regarded Gaming Regulators' European Forum (GREF). GREF has stated that:

'Gambling offered should be restricted to residents of the jurisdiction concerned and residents of such other jurisdictions with whom there are co-operative or reciprocal arrangements.'

105. Effectively, this would require a succession of bilateral or multilateral trade agreements to enable British operators to access overseas players and for operators in those countries to access British customers. This avenue is not without its attractions, but the problems with it can be summarised as follows:

- British based operators will be put at a competitive disadvantage with many existing operators – there must be a good chance that operators would instead locate in other, perhaps less well regulated, jurisdictions offering poorer protections for players irrespective of their nationality;
- It would impose a trade barrier that does not occur with most other types of financial transaction;
- The policing of such restrictions would inevitably be difficult – for instance, an interim report issued in September 2002 by the US General Accounting Office mentioned two ways of compromising credit card coding systems: ' (1) by Internet gambling merchants that attempt to disguise their transactions by miscoding them, and (2) by cardholders who attempt to circumvent the system by using online payment methods;
- It potentially would require the Government or the Gambling Commission to negotiate access and standards with practically every country in the world; and
- For bookmakers it would impose a restriction that they are not presently faced with and one that the Government has not previously considered applying to them.

106. If other jurisdictions wish to prevent their citizens from gambling with British based operators then that of course is open to them. There are numerous mechanisms that they might be able to use, such as restricting advertising or making it an illegal act for the players (eg from 31 May 2002 this approach has been adopted in Hong Kong to combat betting with offshore bookmakers – the penalties include imprisonment for up to 9 months and a fine of up to HK\$ 30,000). Another notable measure applied in both Australia and the USA has been to ask credit card issuing banks to block the cards' use for gambling transactions.

107. Rather than this the Government favours a much more free market approach. This is the preferred option as it is the one that most closely matches the Government's vision of a global market where a well regulated British based industry is able to establish itself as a world leader. Quite apart from that the pitfalls with the other alternatives are there for all to see.

108. For the gambling operators this will mean that there is no 'black list' of countries from where they are unable to accept customers. Instead the responsibility will rest with each of them to make those sorts of decisions based on their individual business profiles. For instance, at present many companies will not take business from the USA. This is either because they respect the wishes of the federal government there, fear possible action being taken if they hold any assets that might be seized, or licences threatened, or risk arrest if venturing into the USA. A similar situation could develop in other

jurisdictions that were also seeking to prevent their citizens from gambling with operators in other states.

109. That cannot be taken to mean that the Government is not supportive of international co-operation. It will be to the advantage of every jurisdiction as there will inevitably be many issues of common interest. The Government should also retain a reserve power to impose geographical restrictions to enable it to review and amend this policy if the situation demands it in the future. For instance, the Government could decide to stop operators from accepting bets from those countries where all gambling or perhaps just remote gambling is not allowed. This may be viewed differently from the scenario where another country is seeking to prevent access by British operators, but where it still permits remote gambling with its own licensed operators. The latter of these would be an attempt to treat the global internet as some form of commercial intranet. While in both cases respecting these countries' preferences and without seeking actively to undermine their domestic policies, Britain will not automatically accept extraterritoriality in this matter. Beyond that it would be for the British courts to determine whether to apply the findings of courts in other jurisdictions.

110. Attempts by other governments to block access to well regulated sites and operators in Britain may have the unwanted effect of driving citizens of those countries to operators in perhaps less reliable jurisdictions. This could not be in anyone's best interests and it is the Government's hope that international standards and agreements could be reached in the longer term.

111. It is appreciated how important state sponsored gambling opportunities are in some countries and it is evident that the UK Government values the National Lottery in the same way. Nevertheless, even there, the Government has not sought to prevent UK citizens from having access to similar online lotteries abroad.

Location of the gambling event/activity

112. In part, the perspective of each state will be shaped by its understanding of where any gambling event is actually taking place. There is no right or wrong answer, but it is something that each jurisdiction will need to decide upon. For example, the US Department of Justice has opined that online wagering takes place simultaneously in both the player's point of origin and the jurisdiction where the gambling operator is based.

113. In Britain we are coming at it from a different policy angle with the presumption that the regulated activity takes place where the operator is based. The reasoning behind this is that player, wherever he is situated, must go to the operator's site to take part in the gambling event and a bet is not struck until it is accepted by that operator. At its most fundamental, the analogy is of an overseas citizen choosing to travel to the UK and gamble in a properly regulated establishment. So far there has been no sign that other jurisdictions will be seeking to prevent their citizens from accessing UK

gambling operators in this manner and yet the only real difference between this and the remote model is one of speed and convenience.

114. Notwithstanding this there are points of principle at stake and both the Government and the Gambling Commission will want to take every opportunity to explain their position to counterparts in other countries. Equally important it would allow them to better understand why some jurisdictions have different policies.

European Dimension

115. Within the European Union gambling legislation is not centrally determined and is left to the competence of each member state. As such each state has developed a unique regime in response to national requirements. There is no harmonisation and in the short term to medium term there is no realistic prospect of this being achieved.

116. For this reason gambling was excluded from the scope of the E-Commerce Directive which came into force in 2002.

117. At a more informal level European regulators or groups of them (eg GREP) will continue to meet and, hopefully, reach common views on various issues. This should be encouraged, but the differences as regard the detailed regulation of remote gambling are such that any consensus will be extremely difficult to reach.

118. There are a handful of European Court of Justice cases (Schindler, Zenatti, Gambelli, etc) relating to gambling products. Due respect will have to be paid to these, but it is far from clear how they could be applied to a comprehensive British based remote gambling industry offering its services on a global basis. It would be perverse if British remote gambling products were freely available all around the world, but because of case law not within the EU. For now it is enough to acknowledge that any British legislation/regulation would have to take account of these rulings.

Taxation

119. An appropriate taxation regime will be essential to the success of the remote gambling sector in Britain. Unlike bricks and mortar operations, remote gambling operators will be in daily competition with offshore competitors. This commercial pressure means that, despite the many attractions of Britain as a jurisdiction and place of business, there will be a level of fiscal cost that would in practice prohibit the gambling operator from being based here. That does not mean there is a case for ultra low taxation levels, but it will need to be a consideration.

120. It is more than understandable that, for planning purposes, this is something that potential licence holders will want certainty about as soon as possible. Unfortunately, both for policy and procedural reasons, Customs & Excise will not be in a position to offer anything explicit until there is greater

certainty about when the new legislation will come into force and how the licensing of operators will fit into the annual tax cycle.

121. Any decisions on that front must quite rightly be left to them to make. They have kept in touch with the evolution of the regulatory policy and are considering the revenue implications. In due course they will no doubt consult both existing and potential operators. Until then a period of uncertainty is unavoidable.

Advertising

122. The bulk of advertising issues apply to all forms of gambling and are being addressed in a separate exercise. That will include, for instance, provisions for preventing advertisers from targeting children and will take into account the provisions of the E-Commerce Directive (although gambling falls outside the scope of the directive, the advertising of gambling does not). Generally, there will be a liberalisation of the advertising of gambling products but there are though one or two points that ought to be made about remote advertising in particular.

123. There are certainly more uncertainties about what exactly constitutes online or telephone advertising. What might be called traditional presentations of advertising, equivalent perhaps to an advertisement in a newspaper are easily identifiable and regulated. Where it becomes harder is in deciding whether items such as hotlinks (icon type features that take someone straight to a gambling site) or even spam (unsolicited e mails) should also be regulated in the same way.

124. Because of this the Gambling Commission must have powers to monitor and restrict the forms and content of related advertisements. This will call for close liaison with existing regulators like the ITC and Advertising Standards Agency.

125. To enforce these powers the Gambling Commission should expect the co-operation of the ISPs, even if they are not held liable.

126. A current anomaly is that while it is illegal to operate online gaming from a British base, offshore operators are free to advertise their services in print and many have done so in newspapers and on billboards. This cannot be allowed to continue and the new legislation will at the same time open up this avenue of advertising for licensed British operators and close it down for non-EEA operators.

Online gambling in non-licensed premises.

127. One effect of the reforms will be to make it safer than it presently is for people to gamble outside of licensed premises.

128. In a sense this is 'private' gambling, but the Government believes that 'public' gambling should normally be restricted to premises licensed for that purpose.

129. The practical difficulties in enforcing this distinction are not to be underestimated, but that is insufficient cause to abandon the policy. The Gambling Review Report (para 30.43 refers) states that:

'The Gambling Commission should have power to take action in relation to premises, not licensed as gambling premises, in which terminals or other facilities are supplied primarily for accessing online gambling services.'

The key word there is 'primarily' and it will shape further thinking on this matter. The aim though is to have the necessary controls contained in the Gambling Bill.

Conclusions

130. The policy outlined in this paper has been shaped by what is currently available in terms of good and bad practice, the views of a diverse range of interested parties and gambling operators, the latest technologies and information sources, and the Government's over-arching vision of how it wants the industry to evolve.

131. Flexibility will be the key to managing the development of a successful British based remote gambling industry. Practical lessons will be learnt and new research will increasingly contribute to a better understanding of the effects of this form of gambling. The Gambling Commission must have the right balance of expertise, resources, and freedom to act in order to build on this knowledge and to react promptly to rectify any weaknesses in the system.

132. While much more detailed work can and should be done by the Gambling Commission in order to introduce a pragmatic, robust licensing and regulatory regime, there should be no doubting that this objective can be met.

133. In moving toward that position it will need to bear in mind the Government's desire to see Britain become a world leader in the field of online gambling and yet, at the same time, be sensitive to any reservations that there may be in other jurisdictions.

134. Effective regulation is by far the most important consideration but, as long as that is not undermined, every effort should be made to appreciate the commercial pressures faced by licensed gambling operators and to help them compete with their competitors in other jurisdictions.



U.S. Department of Justice
Office of Legislative Affairs

Office of the Assistant Attorney General

Washington, D.C. 20530

May 13, 2003

The Honorable Howard Coble
Chairman
Subcommittee on Crime, Terrorism,
and Homeland Security
Committee on the Judiciary
U.S. House of Representatives
Washington, DC 20515

Dear Mr. Chairman:

Enclosed please find responses for the record of the Subcommittee's April 29 hearing on H.R. 21, the "Unlawful Internet Gambling Funding Prohibition Act," pertaining to questions posed by Representative Goodlatte.

I hope that this information is helpful and that you will not hesitate to contact this office if you would like additional assistance regarding this or any other matter.

Sincerely,

A handwritten signature in cursive script, appearing to read "Jamie E. Brown for".

Jamie E. Brown
Acting Assistant Attorney General

Enclosure

cc: The Honorable Robert C. Scott
Ranking Minority Member

The Honorable Bob Goodlatte

**QUESTIONS FOR WRITTEN SUBMISSION ON BEHALF OF CONGRESSMAN
BOB GOODLATTE AT THE CRIME, TERRORISM AND HOMELAND
SECURITY SUBCOMMITTEE HEARING ON HR 21 AND HR 1223
APRIL 29, 2003**

**QUESTION FOR JOHN G. MALCOLM, DEPUTY ASSISTANT ATTORNEY
GENERAL, CRIMINAL DIVISION, U.S. DEPARTMENT OF JUSTICE**

As you know, I have sponsored legislation in the past to prohibit online gambling and to give law enforcement the necessary tools to aggressively prosecute those that violate our gambling laws. I believe that HR 21 goes a long way in combating the problem of online gambling and I am a proud co-sponsor of that bill.

As you know, last November, the 5th Circuit Court of Appeals ruled that the Wire Act, passed in 1961, applies to sports-related Internet gambling and not to other forms of gambling, such as casino-style gambling. Does the DOJ believe that this is the correct interpretation of the Wire Act? Is the prevention of other forms of on-line gambling a priority for the DOJ? What additional tools does the DOJ need to combat both sports-related and other types of on-line gambling.

ANSWER: The Department of Justice has long held, and continues to hold, the position that 18 U.S.C. § 1084 applies to all types of gambling, including casino-style gambling, and not just to sports betting. That being said, we would certainly entertain a proposal to amend § 1084 in a manner that would remove any ambiguity or deficiency that the Fifth Circuit Court of Appeals found in arriving at its decision, and therefore clarify once and for all that § 1084 is not limited to sports betting, and that it clearly applies to electronic and other connections, in addition to telephonic wire communications.

While the war on terrorism and a variety of other pressing crime problems demand much of our time and attention these days, the Department of Justice remains committed to the enforcement of the federal gambling laws to stop all forms of on-line gambling, including both sports and casino-style gambling. While the Department believes that current law generally prohibits Internet gambling, an updating of statutes like § 1084 to take into account current, anticipated, or not yet dreamed of changes in technology would help clarify that the transmission of bets and wagers prohibited by § 1084 remains illegal regardless of how that transmission is accomplished. We thank you for your ongoing efforts to provide law enforcement with tools to battle illegal Internet gambling, including provisions to try to stop the flow of funds to and from illegal gambling operations and deny the Internet services necessary for the carrying on of the illegal gambling. It is provisions such as these that target the services necessary for the survival of the illegal gambling operations that could prove most valuable in actually "starving" the illegal gambling business instead of simply attempting to prosecute them after-the-fact.

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May 6, 2003

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Mr. John G. Malcolm
Deputy Assistant Attorney General
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MAY 08 2003

Committee on the Judiciary

Dear Mr. Malcolm:

Thank you for testifying at the Crime Subcommittee's hearing on bills relating to regulation of internet gambling and for agreeing to answer questions in writing. To that end, I would appreciate prompt answers to the following questions so that the full Committee would have the benefit of your views in advance of reporting any legislation:

H.R. 21, the Unlawful Internet Gambling Funding Prohibition Act, excludes from its definition of "bets or wagers" "any lawful transaction with a business licensed or authorized by a State." During the Subcommittee hearing you indicated that this would "absolutely" allow internet gambling on state lotteries.

- (1) Does the Department believe that current law prohibits all types of internet gambling, including gambling on horse racing, dog racing, or lotteries?
- (2) Does the Department believe that the language, quoted above, would allow internet gambling on horse racing, if the entity was licensed or authorized by a state?
- (3) Does the Department believe that the language, quoted above, would allow internet gambling on dog racing, if the entity was licensed or authorized by a state?
- (4) Does the Department believe that the language, quoted above, therefore, expands legal gambling opportunities on the internet?
- (5) Does the Department believe that the language, quoted above, requires that an entity be licensed or authorized by a state to conduct internet gambling or that it would suffice for an entity to be licensed or authorized by a state for some other purpose?

Mr. John G. Malcolm
Page Two
May 6, 2003

(6) Would the Department support an amendment to strike the language, quoted above, or otherwise clarify that the bill does not weaken the prohibitions in current law on internet wagering?

I would welcome any further explanation you wish to provide. I would greatly appreciate a reply by Monday, May 12, if at all possible. Please reply to B-351-C Rayburn HOB and fax to Ted Kalo at 225-7680. Thank you.

Sincerely,


John Conyers, Jr.
Ranking Member

cc: Hon. F. James Sensenbrenner
Mr. Jamie E. Brown, OLA, DOJ

Note: At the time of the printing of this hearing, no response to Rep. Conyers' questions had been received by the Subcommittee on Crime, Terrorism, and Homeland Security.

