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FINANCIAL ASPECTS OF INTERNET GAMING: GOOD GAMBLE OR BAD BET?

HEARING

BEFORE THE

SUBCOMMITTEE ON
OVERSIGHT AND INVESTIGATIONS

OF THE

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

ONE HUNDRED SEVENTH CONGRESS

FIRST SESSION

JULY 12, 2001

Printed for the use of the Committee on Financial Services

Serial No. 107–34

U.S. GOVERNMENT PRINTING OFFICE

74–100 PS WASHINGTON : 2001

For sale by the Superintendent of Documents, U.S. Government Printing Office
Internet: bookstore.gpo.gov Phone: toll free (866) 512–1800; DC area (202) 512–1800
Fax: (202) 512–2250 Mail: Stop SSOP, Washington, DC 20402–0001

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FINANCIAL ASPECTS OF INTERNET GAMING: GOOD GAMBLE OR BAD BET?

THURSDAY, JULY 12, 2001

U.S. HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS,
COMMITTEE ON FINANCIAL SERVICES,
Washington, DC.

The subcommittee met, pursuant to call, at 2:10 p.m. in room 2128, Rayburn House Office Building, Hon. Sue W. Kelly, [chairwoman of the subcommittee], presiding.

Present: Chairwoman Kelly; Representatives Fossella, Oxley, Cantor, Tiberi, Gutierrez, Inslee, Crowley, Clay and LaFalce.

Also Present: Representatives Leach and Goodlatte.

Chairwoman KELLY. This hearing of the Subcommittee on Oversight and Investigations will come to order. Without objection, all Members' opening statements will be made part of the record.

We convene here today to listen to testimony from two panels of distinguished witnesses about a timely but controversial topic: gambling on the internet. In a few short years, the internet gambling industry has exploded. According to an internet gambling committee of the National Association of Attorneys General, there were less than 25 sites on the web in the mid-1990s.

Today, Bear Stearns, one of the Nation's leading securities firms, estimates that there are between 1,200 and 1,400 e-gaming websites. Bear Stearns projects that as this industry continues to grow, such internet sites could generate an estimated $5 billion in revenues by 2003. That figure approximates roughly one-half of last year's casino earnings in the State of Nevada.

Internet gambling presents a complex set of legal, financial, technical and social challenges. On the legal front, it is believed that most forms of interstate internet gambling are prohibited by Federal law under the Interstate Wire Act. For years authorities have used the Wire Act to combat illegal betting by phone or other wire communications. Now with the advent of internet technology, the Wire Act and other related provisions of Federal law also stand as a legal obstacle against the establishment of internet casinos on U.S. soil.

The most serious offenders in the internet gambling arena are the virtual casinos, operating offshore beyond the reach of U.S. law. One estimate puts the number of foreign jurisdictions authorizing or tolerating internet gambling at 50. This includes not just the well-known bank secrecy jurisdictions of the Caribbean, but other countries like Australia.

The lure of licensing fees and the possibility of sharing in gambling receipts is proving to be a powerful incentive to enter and get other businesses to enter the internet gambling business. Antigua and Barbuda have reportedly licensed more than 80 internet gambling websites already. They charge about $75,000 to $85,000 as a licensing fee for a sports betting site and $100,000 for a virtual casino. A report prepared for the South African government as reported by the Bear Stearns study revealed that internet gaming revenues could yield up to $140 million in foreign exchange.

While internet gambling represents a jackpot for such foreign jurisdictions, it's a wheel of misfortune for far too many Americans who struggle with gambling addiction and the loss of jobs, wrecked marriages and destroyed finances that often follow. With the click of a computer mouse, any American armed with a credit card can have instant anonymous access to round-the-clock gambling from the privacy of their homes. Students on college campuses with nearly unchecked access to credit cards issued by eager credit card companies have already been known to rack up large gambling debts.

As we will hear today, all of the social hazards associated with the problem of gambling at the brick-and-mortar sites are of equal if not greater concern when it comes to online gambling. Furthermore, internet gambling poses a serious problem to our youth. In the areas in which gambling is legal, strict laws have been enacted to ensure our children are prohibited from participating.

In many homes where children are far more computer literate than parents, what possibly is going to stop a child from placing a bet with their parents' credit card? Since our society has made a conscious decision to keep children from this activity, we need to think about taking steps to ensure that online casinos do not victimize our children. The issue of what we can do to protect children from these sites will be one of my first questions for our panelists today.

In addition to the social problems associated with internet gambling, U.S. authorities warn that internet gaming offers a powerful vehicle for laundering funds from illicit forces as well for evading taxes. The use of credit cards and the placement of sites offshore make locating the relevant parties, gathering information for the necessary evidence, and prosecuting those parties difficult, if not impossible.

In closing, let me say that the purpose of the hearing today is one of oversight. It will help us assess what has happened in the internet gambling arena since Congress examined the issue last year. It's my intent, however, not to stop at oversight, but to work with the legislative subcommittees under this subcommittee to support appropriate legislative action in the months ahead.

Internet gambling can no longer simply be left to random events and foreign jurisdictions. It's time for Congress to address these issues and identify an appropriate public policy response.

I would like to let the Members of the subcommittee and the witnesses before us know today that it is my intention to enforce the 5-minute rule, and I would appreciate your cooperation in this. At this time, I am going to recognize Mr. LaFalce.

[The prepared statement of Hon. Sue W. Kelly can be found on page 38 in the appendix.]

Mr. LAFALCE. I thank the Chairlady, and I commend her for holding what I consider to be an extremely important hearing.

I hope that this hearing marks what will be only the first step in this Congress to address the very serious social problems sometimes associated with the expansion of gambling throughout our country and the recurring reliance on gambling in some areas as an economic development tool. I have been concerned for many years with the expansion of high-stakes gambling and was the first House sponsor of legislation that called for the creation of a national commission to study the impact of the spread of gambling on individuals, families and communities.

I was joined at that time by Congressman Frank Wolf, and especially with his leadership in the following Congress, the 95th Congress, we were able to obtain passage of that legislation.

Gambling has become too widespread a phenomenon in American society to eliminate it. We must instead focus our efforts on ways to mitigate its potential adverse consequences on America's families and communities. Gambling can provide a tool for concentrating public and private investment and consumer spending to promote economic growth, so long as it is restricted to a very limited number of jurisdictions. But when it expands virtually everywhere, this ability to concentrate economic resources is lost, eliminated. And this is one of the particular problems associated with internet gambling.

The potential negative aspects of gambling such as excessive debt, bankruptcy, broken families, alcoholism, and other problems will be felt in communities in every part of our Nation without the affected communities realizing any economic benefit or any additional tax revenues to help offset these added social costs. In many instances, the economic benefits of internet gambling go solely to website operators halfway around the world.

I recognize there is a wide variation of opinion within the Financial Services Committee and the Congress on the merits of internet gambling in particular and gambling in general. But I believe and very strongly that internet gambling represents a threat to many of the most vulnerable segments of our population, especially young people who know the medium so well and who are so active in its use.

A dormitory room with one student, one laptop and one or a dozen credit cards can become a virtual casino. And that is true of any room in any building in America or in any country in the world or any place in the world. All you have to do is take your palm wireless out of your pocket and you can engage in gambling anywhere in the world. And how does society benefit from that?

The national commission recommended that Congress act to prohibit wire transfers and other payments to known internet gambling sites. I'm glad that our Subcommittee is examining this issue, and I hope it will lead to legislation putting the commission's recommendation on this subject into statute.

But we shouldn't limit our inquiry to this one area. The commission also recommended that we prohibit the placing of credit and debit card machines and other electronic payment devices in the

immediate vicinity of gambling activities. The commission found that the migration of ATMs and credit card machines inside the casino has been a significant factor in the dramatic increase in problem and pathological gambling. I believe our subcommittee should examine this issue and enact legislation to carry out this other recommendation of the national commission.

In the last Congress I introduced such a bill, H.R. 2811. In the near future, perhaps next week, I will reintroduce that legislation and also legislation similar to the bill that I cosponsored with Congressman Leach in the last Congress to prohibit the use of credit cards and other payment systems to place bets over the internet, but without provisions adopted in the Banking Committee last year that I believe substantially weakened its effectiveness.

I look forward to hearing the testimony of all the witnesses. But I am particularly pleased to welcome Dr. Valerie Lorenz, the Executive Director of the Compulsive Gambling Center, who is an expert in the treatment of compulsive gambling. Dr. Lorenz has firsthand knowledge of the harm created by internet gambling in the lives of individuals.

Madam Chairwoman, again I thank you.

Chairwoman KELLY. Thank you very much, Mr. LaFalce.

We turn next to Mr. Cantor.

Mr. CANTOR. Thank you, Madam Chairwoman. First of all, I would like to compliment you and the staff and certainly Congressman Goodlatte, who has worked long and hard on the issues surrounding the internet and gambling. But I would also like to take this opportunity, Madam Chairwoman, to thank the staff for the quality of the panelists here before us today. One in particular, who is a personal friend of mine, Ms. Penny Kyle, who is here on behalf of the National Association of State and Provincial Lotteries. She is the Executive Director of the Virginia Lottery and a personal friend. She has been in that position at the Lottery for about 7 years in Virginia. It was quite a coup when then-Governor, now Senator George Allen, asked Penny to serve our commonwealth, because she has quite a reputation both in business and government circles. So we felt very fortunate and very lucky to have her in State government making her contribution to the greater good of the commonwealth.

Penny, welcome, and thanks for being here. And I yield back, Madam Chairwoman.

Chairwoman KELLY. Thank you very much, Mr. Crowley. We are going to hear from Ms. Kyle in the second panel and we are glad you are here, Ms. Kyle. Next we turn to my colleague, Mr. Crowley.

Mr. CROWLEY. Thank you, Chairwoman Kelly, for having this hearing today. I want to thank the panels before us. As the former Chairman of the Racing and Wagering Committee—that's a great name for a committee, isn't it?—in the State legislature in New York, I come to the Congress with some background on some of the issues that we are going to be talking about today.

Let me just state that I am a supporter of legalized gambling and would oppose any legislation that would hinder the operations of gaming, whether they be by Native Americans such as the Oneidas in New York or by government entities or by limiting gambling for OTB in New York State or racing in New York State and elsewhere

throughout our Nation where wagering is currently legal. If conducted fairly with adequate public safeguards and by legal adults, I think gaming should be just that—a game—and for leisure.

That is not to downplay the suffering, as has been mentioned, of those who suffer from excessive gambling and addictions caused by gambling, but I don't think we should rush to judgment on a legal and regulated industry because of some tragic examples. In my home State of New York, we have a very well regulated and maintained gaming system which provides hundreds of millions of dollars annually back to the people of the State of New York. And I am very interested in hearing the testimony today.

But I would hope that the subcommittee draw a distinction between and a difference between internet gaming, which I do have concerns for, and the policing of that potential industry, and I have fears, as was mentioned by Mr. LaFalce, for our young and most vulnerable in terms of this new form of gaming. But to draw a distinction between internet gambling and the simulcasting of horseracing throughout the country, an industry in New York State which employs anywhere between 20 directly and 60 thousand people indirectly in the State of New York, the horseracing industry does. And I would hate to see anything done that would diminish that industry in the State of New York. And I would yield back the balance of my time.

Chairwoman KELLY. Thank you very much, Mr. Crowley.

Next we turn to a gentleman who is not a Member of the Subcommittee, but certainly a strong Member of our committee and has a very strong interest in this issue, Mr. Leach.

Mr. LEACH. Well, thank you, Sue. And I want to express my personal appreciation for your leadership on the issue. I have a long statement I would like to ask simply to place in the record.

Chairwoman KELLY. So moved.

Mr. LEACH. And very quickly, just a couple of observations.

Mr. LAFALCE. Jim, could you speak up a bit more? I have difficulty hearing you.

Mr. LEACH. It's my mother's fault, John.

[Laughter.]

Mr. LEACH. Anyway, by way of observations, the Chair and Mr. LaFalce have outlined some of the social implications of this. I would only stress that these implications go far beyond simply the participants in what could be an exponential increase in gambling, because intermediaries have to pick up the cost for losses. Those intermediaries are financial institutions and credit card companies, and they make higher fees for everybody else.

I was a little distressed to read in the testimony we are about to receive that one of America's principal credit card companies thinks this will be too onersome to implement a law that addresses a settlement mechanism. And all I can say is, it would be a lot more difficult to take care of the losses that are likely to arise for these credit card companies. In fact, in my time in the Congress, I would go so far as to say that the conclusion of that testimony understands the vested interest of the industry that it represents less than any testimony I have ever seen.

Having said that, it strikes me that this subcommittee has a special jurisdiction, because we have the most sensible approach to en-

forcement. And the settlement mechanism is the only effective enforcement mechanism I know of for the internet issue. Congressman Goodlatte has helped lead this Congress in looking at new approaches to this issue, and I want to tip my hat to his efforts. But this subcommittee's jurisdiction is very profound on the settlement mechanism issues. And if anyone knows of a better, more effective enforcement mechanism is, I am open to hear about it.

But I would only stress that the approaches that this subcommittee can deal with, and I have reintroduced legislation we introduced last year that passed this committee virtually unanimously, and I might say to the gentleman from New York that it made a very clear distinction between existing kinds of legal gambling enterprises and other kinds of enterprises that aren't legal. But we have an absolute utter obligation to look at this issue on a timely basis, and that means before it gets out of hand. And if one looks at the growth of this industry, it is getting out of hand, and we should act as quickly as possible.

I thank the Chair, and I'm sorry I took more time than I intended.

[The prepared statement of Hon. James A. Leach can be found on page 190 in the appendix.]

Chairwoman KELLY. Thank you very much, Mr. Leach.

We turn now to Mr. Gutierrez.

Mr. GUTIERREZ. Thank you very much. I apologize for the delay. Good afternoon, Chairwoman Kelly and thank you for holding what as I understand is a very important hearing. Today we are joined by a great number of experts who will share with us their knowledge and expertise in the area of internet gambling. I hope that with the information and expertise gathered here today, we would be able to better address the issues concerning the rise of the internet gambling industry.

Approximately one million Americans gamble online every day, and about 4.5 million Americans, about 5 percent of those with access to the internet, have gambled online at least once. Given the substantial number of people directly and indirectly affected by the future of internet gambling, it is our job to guarantee that there are solid laws, secure technology, and high-quality products in place.

Although most States allow some form of gambling activities, many States seek to prohibit online gambling because of the various problems associated with these. These include greater potential for fraud, increase in gambling addictions, protections of State tax revenues and children's easy access to gambling sites. I am particularly concerned about the ease with which children can access cyber casinos. In addition, we need to invest in prevention and treatment programs that will help gambling addicts and their families from devastating impacts of this problem.

As you can see from my opening statement, I am ready to listen to all parties involved, and I look forward to hearing the testimonies so that I can make further decisions. Thank you so much.

Chairwoman KELLY. Thank you very much, Mr. Gutierrez.

We turn now to the Chairman of the committee, Mr. Oxley.

Mr. OXLEY. Thank you, Madam Chairwoman. I want to commend you for calling today's hearing on a topic of utmost concern, the fi-

nancial aspects of internet gambling. While it may seem a good gamble for those who engage in it, experience shows that it is often a bad bet in the end.

Today's hearing is intended to get the lay of the land. We will learn from an economist's viewpoint how internet gambling has grown in recent years. We'll learn from the State law enforcement perspective what power the States have to stop illicit gambling on the web and what means are being taken by criminals to evade those efforts.

We'll hear from those in the trenches, the psychologists and counselors who on a daily basis see the devastation caused by an unregulated industry operating in an unforgiving medium.

We'll hear from the big players in this big game of chance—the large casinos, the State lotteries and the racing industry. And we'll hear from the software providers, the enablers, without whose expertise and acumen internet gambling could not exist. And we'll hear from perhaps the most vulnerable population, college athletics, whose contests become fair game for gambling on the internet, whose athletes are potentially compromised by the allure of cash payments, payouts for throwing games or shaving points, and whose students, your kids and my kinds, are potentially victims of a too easy, snake-in-the-garden enticement of big winnings that often results in financial losses that will trail them and their families for years.

As a matter of fact, just a couple of weeks ago we had a visit from a number of prominent NCAA coaches discussing the problems that have developed over the gambling issue and point shaving and the concerns that they raise. We had everybody from Bo Schembechler, the former football coach at Michigan and my alma mater, Miami University, as well as John Calipari, Lou Holtz, and many, many others.

Finally, we'll hear from the credit card companies, whose products are in most cases the instruments by which internet gambling takes place. I am pleased to see that my full committee colleague and former Chairman of the Banking and Financial Services Committee, Mr. Leach, is in attendance, and I look forward to his questions and comments on this particular issue, since he has had enormous leadership and foresight in this area over a number of years.

The internet to many conjures up the images of the Wild West; the frontier; new, unconquered horizons; seemingly unlimited potential. To those holding such a view, gambling is just part of the tableau. But instead of Gus and Tex sitting at the back table at the Dead Eye Saloon, engaged in a high-stakes game of seven-card stud, we've got little Jimmy sitting at the family computer maxing out mom's credit card. trying to beat the spread on the Ohio State-Iowa game as posted by a virtual casino based in the Netherlands Antilles. Tex and Gus's card game often ended in a little "disagreement," best settled at ten paces in the middle of Main Street. Little Jimmy's losing football bet may result in financial hardship for his family, possible criminal prosecution, and maybe a month without Dawson's Creek for little Jimmy.

If little Jimmy is truly a child, allowed free ability to gamble by some fly by-night casino in the Caribbean or elsewhere overseas, then we have much cause to be concerned. If he is instead Big Jim,

with his pocket full of sports lines, wallet full of MasterCards and Visa cards and access to the casinos of the world through the internet without having to step away from the comfort of his own living room, we have the potential for disaster. Families can be ruined, savings can be lost. In a very real sense, we've gone from "High Noon" to "Wasting Away in Margaritaville."

I look forward to the testimony this afternoon and to continuing dialogue as we tread this thorny but necessary path toward a solution to a troubling and growing threat to our Nation's financial markets and its families.

Madam Chairwoman, again I commend you and look forward to the testimony as this subcommittee completes its first step toward reining in this wild bronco called internet gambling.

Chairwoman KELLY. Thank you very much, Mr. Chairman.

Mr. Tiberi, have you got a statement?

[No response.]

Chairwoman KELLY. Mr. Inslee, do you have an opening statement?

[No response.]

Chairwoman KELLY. All right. Then I'd like to ask unanimous consent. We have with us a Member who is not a Member of our committee but who has a very strong interest in this issue, Congressman Goodlatte. And Mr. Goodlatte, have you any opening statement?

Mr. GOODLATTE. Madam Chairwoman, I just want to thank you for holding this hearing and second to thank you and the other Members of the subcommittee for your indulgence in allowing me to participate today. This is an issue that I have a great deal of interest in, introduced legislation in the last Congress which received the vote of 61 percent of the Members of the House. A companion bill introduced by Senator Kyl in the Senate has passed the Senate on two occasions. And so this year we want to work very closely with your subcommittee and your concerns regarding the financial instruments used here to formulate legislation which will be passed and address this problem.

It's a serious problem of literally billions of dollars being sucked out of our economy by hundreds of illegal, unregulated, untaxed, offshore entities that are causing problems in communities just as if the community, had a casino in their downtown, all of the problems that come, family problems, criminal problems, addiction problems, bankruptcy, all of those things occur with this just as if you had the problem right in your community.

So we as a country have an obligation to address this problem, and I thank you for your leadership in holding this hearing today to get us started on the information we need.

Chairwoman KELLY. Thank you very much, Mr. Goodlatte.

Mr. Fossella, did you have an opening statement?

Mr. FOSSELLA. I'm still trying to digest what Chairman Oxley said.

[Laughter.]

Mr. FOSSELLA. So I don't have a statement.

Chairwoman KELLY. Thank you very much. If there are no more opening statements, let's begin with our first panel. We'll begin first with Mr. John Peter Suarez, the Director of the Division of

Gaming Enforcement for the New Jersey Department of Law and Public Safety, who has recently brought suit against three offshore casinos, focusing on their billboard advertising and targeting of minors.

Next we have Mr. Sebastian Sinclair, Vice President of Christiansen Capital Advisors. He is an economist who will discuss the money involved in internet gambling and the increasing number of internet gambling sites and give his view of where things are going in the future.

Then we will hear from Mr. Keith Whyte, the Executive Director of the National Council on Problem Gambling Incorporated, who represents counselors who deal with problem gambling, including internet gambling.

Next we will listen to Dr. Valerie Lorenz, the Executive Director of the Compulsive Gambling Center, who is a psychologist who treats compulsive gamblers, including internet gamblers.

Finally, we have Mr. Frank Fahrenkopf, President and CEO of the American Gaming Association, which represents casinos, who will share their perspectives on these issues.

I want to thank all of you for taking time out of your busy schedules to join us here today to share your thoughts on this important issue. Without objection, your written statements will be made a part of the record. You will each be recognized in turn for a 5-minute summary of your testimony. Thank you very much. And we'll begin with you, Mr. Suarez.

STATEMENT OF JOHN PETER SUAREZ, DIRECTOR, DIVISION OF GAMING ENFORCEMENT, NEW JERSEY DEPARTMENT OF LAW AND PUBLIC SAFETY

Mr. SUAREZ. Thank you, Madam Chairwoman and Members of the subcommittee. I appreciate very much the opportunity to speak to you today about internet gaming.

Before addressing directly internet gaming, I would like to give you a brief synopsis of gaming as it exists in New Jersey today. Gaming was first legalized in New Jersey in 1977, and we opened our first casino shortly thereafter in 1978. Since that time, 12 casinos have opened in New Jersey, and those 12 casinos employ roughly 50,000 people in our State. Those 12 casinos generated $4.4 billion in revenue last year and received over 34 million visitors, making it by some accounts one of the most popular destination resorts in the United States. The internet could change all of that.

By our estimates, and Madam Chairwoman, you alluded to this, there are well over 1,000 internet sites located predominately in offshore locales such as Antigua, the Netherlands Antilles or other Caribbean countries. The typical internet casino, though quote/unquote "licensed" by the host country faces none of the regulatory scrutiny that is typically associated with land-based casinos. Indeed, it is our view that many of the operators of offshore casinos seek out jurisdictions with the lowest common denominator of regulatory scrutiny, moving their operations from places where they are not subject to strict Government oversight.

The risks of unregulated internet gaming, or rather poorly regulated internet gaming, should be clear to every Member of this sub-

committee: No meaningful limitation on participation by underage gamblers or problem gamblers. No assurance as to the integrity of the operators or the game or to the fact that payouts will actually be received. The concerns regarding money-laundering. Protection against security breaches, hacking, and information oridentity theft, to name some of the more salient concerns.

From an economic standpoint internet gaming as it exists today fails to provide any positive benefit to the United States in the form of income taxes or taxes or jobs. In addition to those concerns, from New Jersey's perspective, the fundamental problem with internet gaming is that it is a violation of New Jersey's Constitution. Our Constitution requires any form of gambling to be specifically approved by the people by a vote in a referendum. The question of internet gambling has never been put to the people of New Jersey and therefore represents a violation of our Constitution and our civil and criminal laws.

Faced with this industry, New Jersey has instituted legal proceedings against three internet operators to stop them from soliciting or accepting wagers in New Jersey. In June of this year, the Division of Gaming Enforcement, the agency of which I am the director, took the unusual step of filing civil complaints against three internet casinos that were operating and advertising in New Jersey. These three were identified because of their billboard advertising and because of the ease with which we could wager.

Two of the sites offered sports book and casino-style games. The third offered just casino-style games. All three accepted wagers from 15-, 16- and 17-year-old children without any screening mechanism whatsoever. In our action, we have asked the courts to enjoin these casinos from accepting wagers from New Jersey residents and to recover funds lost by our citizens.

Although we fully believe that our cases can and will be won, they will present some difficult issues for the courts to address, and those issues will take time. One of those issues that I would like to touch on briefly is the question of jurisdiction. As many of you Members know, many of the offshore operators contend that since they operate in an offshore locale where they are legally entitled to operate and the wagers are processed in that offshore locale, they do not have any concerns nor does the States or the Federal Government have any jurisdiction over them. This argument is quite simply nonsense.

And as far back as 1953, New Jersey Supreme Court recognized that a wager takes place both where the call is made and where the call is received. That theory of jurisdiction has been applied in just about every case that's been asked to address internet gaming in the United States. That is the same as the policy of the Department of Justice and has always been that case.

Once we defeat claims about jurisdiction, however, we must deal with the difficulty of processing or proceeding in a civil context. In the time that it takes us to proceed, more casinos will open up, more wagers will be accepted, more money will be lost.

Before I mention the legislation and sum up, I would like to say that in testifying today, I do not intend to advocate for or against a referendum in New Jersey. I do intend, however, to be advocating that some action must be taken. There are obviously two choices

facing the States and the Federal Government: They are prohibition or regulation. Obviously, regulation can and could be done along the models at land-based casinos. Prohibition along the lines of the Leach-Kyl-Goodlatte provisions that simply declare credit card debts or other transactions that are a result of illegal internet wagering can and will be enforced if that legislation is passed.

I submit to you that something can be done. The time to do something is now. Because this is, from New Jersey's perspective, a far too important issue to be decided by inaction. And I do not believe that the mistaken belief in the impossibility of enforcing a prohibition should be the basis from which a rational decision about internet gaming should be made.

Thank you for the opportunity for speaking to you today, and I am available for questions if you have any.

[The prepared statement of John Peter Suarez can be found on page 61 in the appendix.]

Chairwoman KELLY. Thank you, Mr. Suarez.

Mr. Sinclair.

STATEMENT OF SEBASTIAN SINCLAIR, VICE PRESIDENT, CHRISTIANSEN CAPITAL ADVISERS

Mr. SINCLAIR. Good afternoon. To answer your first question, which was whether internet gambling is a good gamble or a bad bet, I'm sorry. I don't have the answer to that.

This is an intractable problem that has imperfect solutions. As Mr. Suarez mentioned, we have the option of prohibition versus regulation. There is no magic bullet here. But let's look at the state of the industry as it exists now. We estimate that $2.2 billion was spent globally on internet gambling last year.

The interesting aspect of that is that the majority of that came from U.S. citizens. And in keeping with the theme that we're talking about here today, another majority of that, about $1 billion, was probably bet on sports, which based upon the Cohen case, which probably appears several times in the written testimony, is illegal in this country. Of that $1 billion that was bet on sports, about $700 to $800 million probably came from U.S. residents. This is what would be a prohibited activity in this country, based upon the Cohen case.

Now let's look at what the Cohen case tells us. Mr. Cohen was convicted of violating the Wire Wager Act. It is currently on appeal. Most legal scholars who are familiar with the Wire Wager Act don't expect him to win that appeal. So while the Cohen case was a legal victory, it was a practical failure. And it was a practical failure for two reasons. One, Mr. Cohen voluntarily came to the United States to stand trial. And two, his company, World Sports Exchange, is still operating and is still taking bets from U.S. citizens.

Now as we move into the option of prohibition versus regulation, in my perspective as an analyst and looking back at history, we have been relatively unsuccessful in the past at legislating away demand. In previous eras we used to be able to do it by restricting supply. As some of the Members mentioned today, gambling has expanded in this country to the point where today it is now a $61.4 billion business.

Stopping supply is difficult in the Digital Age. It is difficult, as some of the legislation has proposed, to block access to gambling sites. As we'll get into a little further on, choking financial transactions, which seems to be the legislative frontrunner and probably the reason why we're here today, has enforcement problems as well.

The first thing that we need to talk about is that you can argue whether gambling is right or wrong, moral or immoral, but the fact is it's pervasive. I don't know the local area very well, but I imagine that I don't have to walk very far to buy a DC. lottery ticket. Eighty miles from here to the East, I can play the slot machines at Dover Downs or at Harrington Raceway. And Washington, DC. is not unique. In any other location in this country, I could probably make similar statements.

So the question is, how do we un-ring that bell? Through sucessive expansion we have created demand for a product that is today available in an unregulated environment.

So then we move on to the enforcement problem. Speaking specifically to the credit card issues that we're talking about here today, I see two problems with that in terms of enforcement. One is getting foreign countries and banks to devote time and resources to what is a legal activity in their jurisdictions. The United Kingdom and Australia actively seek bets from U.S. citizens. In fact, legislation was just passed in Australia that allows them to do so.

The second problem, and I see that as more of a real problem, because maybe the Government will be successful at getting foreign-based banks to stop processing those transactions. This other problem is the PayPal problem. The third-party transaction processors. PayPal is a company that uses digital cash. You can set up an account with wire transfer, check, or credit card, and you can use that digital cash at any site. I call it the PayPal problem, because that's probably one third-party processor that you're familiar with. But in the very near future, if this legislation, as I see it, were to pass, it would create a whole new illegal industry, and that's third-party internet gambling processors located in offshore jurisdictions.

So let's explore the other option, regulation in a legal context. The medium of the internet lends itself to regulation. Let me give you a quick example. The Western European model of legalizing internet gambling is to restrict it to the Nation in which it is located. And there are very good ways to do that. One way that is being proposed and actually being utilized is a proprietary dialer that will only dial seven digits from where you are. It works. It's 100 percent effective. The technology has been approved by the Nevada Gaming Control Board, and it effectively restricts access to gambling sites from one location. Conversely, it's very difficult to restrict gambling sites from coming in. And I'm out of time.

Chairwoman KELLY. You can sum up if you want.

Mr. SINCLAIR. OK. Real quickly.

Chairwoman KELLY. OK. That's enough.

[Laughter.]

Chairwoman KELLY. Just kidding.

Mr. SINCLAIR. In conclusion, I've been following this industry for a long time, and I can understand the fears associated with gam-

bling and the spread of gambling. But I am always reminded of the old adage to keep your friends close and your enemies even closer. Gambling is a product like alcohol that is dangerous to some. There are very real dangers associated with gambling. But it's my belief that sweeping this activity under the rug and handing it to criminals will do more to exacerbate problem gambling than to help it.

[The prepared statement of Sebastian Sinclair can be found on page 84 in the appendix.]

Chairwoman KELLY. Thank you, Mr. Sinclair.

Mr. Whyte.

STATEMENT OF KEITH S. WHYTE, EXECUTIVE DIRECTOR, NATIONAL COUNCIL ON PROBLEM GAMBLING

Mr. WHYTE. I would like to thank the Chair and the Members of the subcommittee for the opportunity to testify on behalf of the National Council on Problem Gambling, the Nation's oldest and largest organization dedicated to addressing problem gambling issues.

Since 1972, we have worked with Federal, tribal, State and local governments, the gaming industry and other non-profits to address problem gambling. The mission of the National Council is to increase public awareness of problem gambling, to ensure the availability of treatment for problem gamblers and their families, and to encourage programs for research and prevention.

We have consistently maintained a position of neutrality on gambling, arguing neither for nor against it. We currently have 33 State affiliates throughout the Nation, and numerous corporate and individual members. We are the leading United States experts on problem gambling treatment, prevention, research, and education.

Pathological gambling is a mental health disorder. I've attached the standard criteria from the American Psychiatric Association to my testimony. Prevalence-wise, about 1 percent of the U.S. adult population would meet criteria for pathological gambling in a given year. Another 2 to 3 percent would meet criteria for problem gambling, which is the less severe but certainly folks that are experiencing problems relating to their wagering.

Now 2 to 3 percent doesn't sound like a lot. In real terms, that translates to 11 million Americans that are facing problems with their gambling each year.

As several Members have noted, not surprisingly, problem gamblers suffer from a high rate of financial debt, suicide, mental health problems and other physical disorders, and bankruptcy are all associated with problem gambling.

Gambling on the internet is a relatively new issue, and I would like to present a little bit of evidence that we have. Unfortunately, the research in this area has lagged behind the public policy debate. A recent study in Oregon shows that of 14 forms of gambling, legal and illegal gambling, only one has grown between 1997 and 2000. That is internet gambling. If you average it out, the growth rate in percentage terms, it's 91 percent a year.

And although internet gambling has been growing rapidly, as many of you have noted, legalized gambling in the U.S. participation-wise has stayed relatively the same. Anywhere from 75 per-

cent to 80 percent of U.S. adults will place a bet at at least one point in their lifetime. And I think that's a significant number for the subcommittee to recall in that legalized gambling and gambling participation is in essence ubiquitous throughout the United States.

As Chairwoman Kelly and Representative LaFalce have noted, a particular area of concern is the intersection of three trends: Access of adolescents to the internet, access of adolescents to credit, and the propensity of adolescents to bet on existing areas. Surveys show that participation by adolescents is sky high. Over 40 percent have played card games for money in the past year. Thirty-two percent have bet on games of skill such as pool or golf. Thirty-one percent have bet on sports, and 30 percent have bet on the lottery. It is significant to note that not only are all four of these activities illegal for adolescents in the United States, but these surveys were based on telephone surveys from home. So we can anticipate that the adolescent at home answering these questions is possibly going to underestimate their involvement.

Furthermore, youth have access to credit. A Consumer Federation of America survey found that over 70 percent of undergraduates have at least one credit card. We certainly know that this same population has enormous access to the internet. We are increasingly concerned that this cluster of trends is going to result in a lot more internet gambling among adolescents.

I took a sample of 18 calls from our nationwide help line that we have received over the past 4 months. Significantly, four of those 18 callers to our help line were students between the ages of 18 and 25. I have reproduced the statistics on my chart at the end of my testimony, which I would encourage you to examine. It is important to note that this survey is neither representative of callers to our help line nor of problem gamblers in the United States, nor of gamblers anywhere else. It's an extraordinarily small sample, only about 2 percent of our intakes.

But what we'd like to make sure that this subcommittee has a perspective of is the enormous damage that is already occurring from internet gambling and from legalized gambling in the United States. The primary concern of the National Council on Problem Gambling is not so much the increased accessibility of the internet, but the fact that even for people that have problems with legal gambling in the United States, there is simply nowhere for them to go. All 18 of those callers to our help line have an 80 percent of being denied insurance coverage for their gambling addiction. There are only 15 States that provide any sort of services for people with gambling problems.

We would encourage the subcommittee, as you are wrestling with the difficult issue of internet gambling, to realize that problem gambling extends beyond the internet to those who already are gambling on legal activities in the United States. But we thank you very much for the opportunity to testify, and we will be happy to answer any questions.

[The prepared statement of Keith S. Whyte can be found on page 109 in the appendix.]

Chairwoman KELLY. Thank you very much, Mr. Whyte.

Dr. Lorenz.

STATEMENT OF VALERIE LORENZ, Ph.D., EXECUTIVE DIRECTOR, COMPULSIVE GAMBLING CENTER, INC., BALTIMORE, MD

Ms. LORENZ. Thank you for permitting me to testify as well.

Chairwoman KELLY. Excuse me, Doctor, would you please pull that microphone closer and raise it so that we can hear what you're saying? Thank you.

Ms. LORENZ. Thank you. First of all, I would like to thank this subcommittee for permitting me to testify as well. Briefly, I have been in the field of compulsive gambling for nearly 30 years, and in that time, I have seen gambling increase from the State of Nevada, which had pervasive gambling, to now all forms of gambling in virtually every State except three, all the way up to the internet. We have indeed become a Nation of gamblers.

I was asked to respond to four specific questions: "What impact has the internet had on the problem of underage and pathological gambling?" Well, that's an interesting question, but it is hard to quantify, because there is no hard data. We have not had the research monies to really respond to that question in a scientific way. I can tell you, though, that as legalized gambling has increased, so has the number of compulsive gamblers.

To add to the figures that we see in various studies which state anywhere from 1.5 to 5 percent of the people of the American adults are compulsive gamblers, depending on the amount of gambling in a particular State, we also have those people who are considered problem gamblers, those who do not yet meet the criteria of gambling addiction but who are on the verge of that addiction if they continue to gamble.

The largest increase that we see among compulsive gamblers are the teenagers, the young people, those in their early twenties, and our senior citizens. The question is, what is the impact of compulsive gambling? One needs to remember that gambling is an addiction, and just like alcoholism, gambling addiction will continue into future generations. This is not only the gambling itself, but also the impact of compulsive gambling. It will continue into future generations. That is the nature of addictions.

Compulsive gambling leads to financial ruin, severe indebtedness, and to bankruptcies, to poor work productivity and terminations, to broken homes, broken families and lost homes, to health problems and other addictions, not just among the gamblers but also among the gamblers' families.

It has a frightening suicide rate. And crimes which in the past were non-violent financial crimes, have now expanded to crimes of violence, including homicide.

We have a larger population of senior citizens than we have ever had before in our country. Usually on a monthly basis, these seniors will take a bus to the casinos or buy daily lottery tickets. Now we are proposing that they stay at home and gamble over their TV and computers. In short, they can lose everything they have ever worked for, lose it in their own living rooms with no chance of financial recovery, or in many instances, survival.

For the first time in our country, we have an entire generation growing up with Government's message that gambling is OK. This young group of people has been schooled on computers. Many have

their own laptops. They can log onto AOL, pull up Pogo, where half the 40 choices of games are gambling games. It is this young population that now is being hooked. It is so easy to forget the time spent on a computer and not to realize how much money has been put on a credit card. All these tools are products of gambling.

According to the Internet Gaming Council, a trade association, it has tracked 1,400 websites that invite people to gamble. Internet gambling would increase this number dramatically if it were to be legalized.

Second question: "What technical obstacles stand in the way of these issues? Regulation?" I would say there is no way to regulate gambling on the internet on one's computer or television. Quote: "It's not just feasible for law enforcement to monitor what people are doing in their living rooms with their computers," says John Glogau, Special Counsel to Florida Attorney General Bob Butterworth. Does this country really want citizens who can gamble away their savings on the internet?

The third question was, "What steps has the National Council on Problem Gambling taken to date to curb the abuses associated with internet gambling?" Mr. Keith Whyte told you some of those things. I don't know the whole question. I resigned from the National Council due to philosophical differences many years ago. I do know that there is a strong cooperation of the National Council with the casino industry.

The fourth question was, "What recommendations do you have for this subcommittee on steps Federal and State authorities should take to address internet gambling?" First of all, I would recommend, as also recommended by the National Gambling Impact Study Commission, putting a moratorium on all expansion of legalized gambling, including internet gambling.

Chairwoman KELLY. Dr. Lorenz, if you could sum up, please, we would appreciate it.

Dr. LORENZ. Thank you. I further recommend that the governments and Congress address all the issues and public policy relative to legalized gambling and compulsive gambling, recognize the escalation of gambling addictions, provide the funds through top-level administrative support just as you've done with alcoholism and drug addiction. Fight compulsive gambling, don't condone it. I would be happy to answer any questions.

[The prepared statement of Dr. Valerie Lorenz can be found on page 123 in the appendix.]

Chairwoman KELLY. Thank you very much.

We turn now to Mr. Frank Fahrenkopf, Jr. We appreciate your being here, sir.

STATEMENT OF FRANK FAHRENKOPF, JR., PRESIDENT AND CEO, AMERICAN GAMING ASSOCIATION

Mr. FAHRENKOPF. Thank you, Madam Chairwoman. The American Gaming Association is the national trade association of the commercial casino industry. Our members are the companies with household names to many, such as Harrah's, MGM Mirage, Mandalay Resort Group, Park Place Entertainment. We operate land-based and riverboat casinos in 11 States across the country.

Consideration of questions about internet gambling we believe must be viewed in light of the nature of gaming and how decisions about public policy issues concerning legal wagering have been handled ever since the founding of this Republic and we believe should be continued to be resolved that way in the future.

As the National Gambling Impact Study Commission reaffirmed in its final report in 1999, except for certain limited areas, such as internet gambling and Native American gaming, States, not the Federal Government, should decide whether to permit legal wagers by persons within their States, and if so, how to license those in the wagering business and how to tax and regulate their operations.

Our major concern with internet gambling as it exists today is that it allows offshore websites that accept bets and wagers to frustrate important State policies, including restrictions on the availability of gaming within each State. Similarly, unregulated internet gaming that exists today allows an unlicensed, untaxed, unsupervised operator to engage in wagering that is otherwise subject to stringent Federal and State regulatory controls. These controls are vital to preserve the honesty, integrity and fairness that those in the gaming industry today have worked so hard for so long to bring about.

The importance of this concern cannot be overstated. As the U.S. Department of Justice has stated before Congress on several occasions, the law should treat physical world activity and cyber activity over the internet in the same manner, whether it comes to gambling or otherwise. As the Justice Department pointed out in testimony to the Senate Indian Affairs Committee in 1999, and I quote, "If activity is prohibited in the physical world but not on the internet, the internet will become a safe haven for that criminal activity", unquote.

In addition to State level restrictions on where legal wagering may take place, and extensive licensure and regulation of those who engage in the business of taking legal wagers, there are important Federal requirements applicable to commercial casinos and other forms of legal wagering in this country. For example, U.S. commercial casinos are subject to Federal corporate taxation. Publicly traded companies comply with financial disclosure and other Securities and Exchange Commission rules. Casinos file information reports on larger winnings with the IRS and withhold Federal taxes on certain winnings.

And casinos, very importantly, adhere to anti-money-laundering statutes and regulations administered by the U.S. Treasury Department's FINCEN Division. By contrast, those engaged in the business of illegal internet wagering in the U.S. from offshore are not subject to U.S. law enforcement jurisdiction on these important matters of public administration.

Now while the AGA could support appropriately drafted legislation to update Federal statutes to preserve the traditional policy of State regulation, any changes to Federal or State laws in the pursuit of making internet gambling illegal need not and should not be drawn so broadly as to lump the use of technology within otherwise legal limits in the same prohibited status as those who are doing so outside State law.

This position is consistent with the policy of the Wire Communications Act, which since the 1960s permits the use of the wires for wagers and information, assisting in the placing of wagers, where the transactions are entirely intrastate or between States in which the wagering in question is legal.

In other words, there is a difference between using technology to circumvent Federal and State restrictions and regulations as is done today by those operating offshore internet gambling sites, and the use of technology by licensed operators to more efficiently deliver their services where, to whom, and under what conditions they are authorized by Federal and State law to do so.

There are clearly understandable enforcement concerns that this subcommittee must deal with. But it is important also to point out that the commercial casino industry has been at the forefront of tackling the difficult problem of pathological gambling that some of the other witnesses have testified to. The National Gambling Impact Study Commission actually commended our industry for its work in being the primary funder of research on this disorder. And I ask you to go back and look at that Commission report. A lot of people have been throwing things around like bankruptcy and crime and suicide and divorce. That's not the findings of the National Gambling Impact Study Commission, except to that 1 percent of the population who are defined as compulsive and pathological gamblers.

The position of the AGA is that we continue to oppose unregulated internet gambling, because we believe the technology does not currently exist to prevent underage gambling, to protect against pathological gambling, and to permit the strict regulation and law enforcement oversight required for integrity.

Thank you very much, Madam Chairwoman.

[The prepared statement of Frank Fahrenkopf can be found on page 137 in the appendix.]

Chairwoman KELLY. Thank you very much. And thank you for staying within the time limit.

I want to just ask a couple of questions. We are going to ask a few questions, then we are going to go vote. We will come back to finish.

Mr. Suarez, as I understand it, during your investigation of offshore internet gambling, 15- and 17-year-old kids were able to set up accounts and place bets from computers in New Jersey. Is there anything we can do to prevent minors from having access to an offshore casino?

Mr. SUAREZ. Madam Chairwoman, we were able to have those underage kids gamble. And the real obligation to do that screening really falls on the operators themselves. In these cases that we had, we had the children enter their correct birth dates. And on two of the sites, they were told—the site reported back that they were underage, and changing only the age description in the field, the child simply said, "I'm 21", and he was allowed to wager and place wagers on those games.

In the other circumstance, we were actually just told, don't come in if you're under 18, and we clicked on the screen, "I agree that I am over 18", and we got right in. There is nothing except for the technology that may permit parents to screen certain ISPs or cer-

tain home pages that could be done. But the operators can simply avoid that by identifying their screen in a different way.

The screening software, the nanny software, requires cooperation from the operator and the parents.

Chairwoman KELLY. Thank you. I just want to follow up with one question about the fact that law enforcement authorities have talked with me and raised some concerns about the potential for money laundering and other financial crimes in connection with internet gambling. Can you explain how internet gambling lends itself to money laundering?

Mr. SUAREZ. Probably the easiest way that we can see it is that there is no guarantee on the side of the house, the internet casino, that they are complying with the reporting requirements of Federal law, be that for cash deposits, cash transactions, or the movement of money to and from other accounts that may be offshore through to the accounts themselves.

The most common way that an internet casino pays a wager is that they can credit up to the amount that a person originally put down, then they send a check in the mail. And so there is no way that we in the United States can track how many transactions, where the money is coming from, any paper trail that we can go to to these internet sites, because we simply don't have the ability to capture the information or to guarantee that those casino sites, internet sites, are properly capturing information that they would be required to capture were they a land-based operator.

Chairwoman KELLY. Thank you very much. Dr. Lorenz, I would like to know if you would be willing to share with us, in generalities if necessary, any cases that you have worked with involving internet gambling.

Dr. LORENZ. Yes, Madam Chairwoman, I can tell you of a current case. This is a police officer who served very commendably in a nearby county, a very large county, also very large police department. He had a very stressful job, and he went to gambling on the internet in order to relieve that stress.

I had hoped to bring him here today, but he is facing legal charges, and his attorney suggested it was not a good idea at this time. You can imagine that this police officer is extremely embarrassed because the men he worked with for 30 years now have to arrest him and take him to prison.

I have a paper here. We have our patients fill out a sentence completion form. Let me just read some of the sentences that he completed. "I think gamblers are"—and he says, "sick people who haven't realized their sickness." And that is very true.

"I am fearful of my future until I get help." This is a man who for 30 years was a police officer. "I am not going to commit suicide," although he had tried, and the last thing that stopped him is that his fellow officers would find him.

"Most people don't know that I tried to stop gambling many times."

Question five: "The most unusual experience I have ever had while gambling," was using other people's money. He stole over $100,000 from his police department.

Question six: "People who see me when I am gambling think I am just playing on the internet."

Chairwoman KELLY. Thank you, Dr. Lorenz. I appreciate that.

Dr. LORENZ. One more question? One more statement?

Chairwoman KELLY. I've run out of time. I appreciate it. I am going to turn to Mr. Gutierrez, and if you would like to continue this, please do.

Mr. GUTIERREZ. Sure. I just have a couple of questions to Mr. Peter Suarez, John Peter Suarez.

In Mr. Fahrenkopf's written testimony, he basically says that he's not concerned about internet gambling in terms of competition from internet gambling because he cites that they go for the hotels and all the excitement and everything else that goes along with gambling.

However, you have mentioned in your remarks that the rise of internet gambling could threaten the success and reduce revenues of those strictly regulated casinos in Atlantic City. Could you explain the difference?

Mr. SUAREZ. New Jersey's gaming market is unique in that gaming in New Jersey is limited to the city of Atlantic City and cannot take place anyplace else. So if you want to gamble, you must come to Atlantic City to one of the 12 licensed casinos, unlike Nevada, where gaming is pervasive throughout the State. I don't want to speak for Mr. Fahrenkopf, but I believe that is the distinction in that the operators in New Jersey have committed substantial resources and investment in developing Atlantic City.

And for a patron who ordinarily would drive down the parkway or the Atlantic City Expressway to come, if they could avoid that by simply logging on, then I think by all accounts, we don't know the extent of the impact, but I think we all recognize that there would be a negative impact in the gaming market in New Jersey.

Mr. FAHRENKOPF. Mr. Gutierrez, the average stay in Atlantic City is something like 10 hours. The average stay in Las Vegas is 3 days.

Mr. GUTIERREZ. OK.

Back to Mr. Suarez. If prohibition of internet gaming was chosen as the course of action by the State or Federal Government, how could this prohibition be enforced?

Mr. SUAREZ. The prohibition would have to be accompanied by the tools that you have identified, which is, as the National Gambling Impact Study Commission recommended, to simply make wagers that are placed over the internet and the obligations associated with those uncollectible in the United States. That simple declaration of policy and laws to that effect would render I think the profitability of internet gaming—it would render it virtually unprofitable if an operator could not effectively come to the United States and try to collect that debt, because that debt is unenforceable in the courts in the United States.

Mr. GUTIERREZ. And following up with Sebastian Sinclair, if prohibition as you've emphasized throughout your written statement, would be very hard to enforce, and you suggested, quote, "may be a poor policy choice for internet gaming", then what would be the right, foolproof choice for the Government to protect individuals interested in internet gaming.

Mr. SINCLAIR. Well, I think I answered that when I stated that there is no foolproof answer as I see it.

This legislation assumes a debt-based transaction. Credit cards are not the medium for this industry, and they never will be, because gambling debts already are uncollectible in a great portion of the First World, the State of Michigan, for instance. You'll simply be pushing it to different mediums of exchange.

Now the way I see it, as I said before, keep your friends close and your enemies even closer; there is no good answer, but there is a lesser of two evils. And I think a real concern and a real problem that is associated with gambling is problem and pathological gambling as we've heard about a lot on this subcommittee.

But it is my opinion and my belief that by trying to prohibit this activity in a way very similar to the Volstead Act, the cure will be worse than the disease. You can't legislate away demand, and on the internet, it's difficult to legislate away supply. You're going to hand this industry to suppliers who aren't concerned about problem and pathological gambling, and it's going to maintain.

Mr. GUTIERREZ. Well, we don't want to gamble any more with the time we have to go vote. I think we have 4 minutes and we're both pretty healthy and swift, but let's get over there to vote. We'll be right back. Thank you.

Chairwoman KELLY. Thank you. We will take a 10-minute break and resume.

[Recess.]

Chairwoman KELLY. Thank you very much. I apologize for such a long delay. May we have our witnesses back?

I understand Mr. Fahrenkopf had to leave. We will have to give him some written questions. But since I have completed my questions, with unanimous consent, Mr. Leach, would you like to open your line of questioning?

Mr. LEACH. I don't have exactly any questions for the panel, but I would like to read a very brief long sentence or two sentences, because it relates to some things that have been said with regard to several of the comments about the possibility that third party intermediaries such as PayPal may obviate the effectiveness of legislation like H.R. 556 that makes it illegal to use financial instruments for illegal internet transactions. Let me be clear that H.R. 556 also makes it illegal to use the proceeds of credit or to extend credit on behalf of any other person or to use the proceeds of any financial transaction for illegal gambling.

What this means is that third party intermediaries like PayPal would be captured under the enforcement mechanisms of the Act. Now PayPal kinds of transactions would be treated the same as direct credit card transactions. And I just want to stress that this particular kind of effort to get around the prohibitions of the Act, I don't think, would be very effective.

Second, several people have asked me something about my opening statement that related to the Visa testimony to come. And we are going to be under some very awkward time constraints on some voting. So let me just make it clear what I was getting at. I am nothing less than astonished that a credit card company, of all kinds of companies, would testify that it objects to these kinds of payment mechanism approaches. Because what is at issue here for credit card companies is not simply the legal subtleties of how you comply, but the fact if you don't have this situation, you are going

to massively increase the number of bankruptcies in America. You are going to massively increase the number of credit card indebtedness, and nothing could be less advantageous to the vested interest of a credit card issuer. And so it is my personal view that of testimony I have read, I have never seen testimony that is less in the vested interest of the party that is projecting it.

And having said that, I would also say, I am absolutely astonished at the lack of interest to date of the financial intermediary community. And by that I mean America's banks, America's savings and loans, America's insurance industry. Every single one of these industries has a spectacular interest in not seeing the problems in American society that are beginning to evidence themselves.

I cannot think of a higher priority for the American banking industry than legislation of this nature. And it is just extraordinary the silence that has greeted it, both in the last Congress and this Congress. And I think that the American Bankers Association, the Independent Bankers Association, the insurance industry have really got to look at these circumstances and come to a conclusion what's in the best interest of American society and what's in the best interest of the financial well being of American civic life. And I think we have to be very concerned.

When the Chair reads a statistic that says that a million people gamble a day, I would stress in a society of about 300 million people, that that isn't 1 million people one day and another million people the next, it is a million people that repeat and repeat and repeat. And given the odds that exist in gambling, the greater the amount of volume of gambling, the greater certainty is of the greater the loss. The odds are against the public. And I think it's an absolute duty of the United States Congress to say that the public ought to be protected from odd circumstance that are stacked against it.

And I want to say to this panel, I am very appreciative of the testimony of many of you who are deeper into this subject than I have ever been and have seen first-hand results of a very deep nature.

But my concern, Madam Chairwoman, is that the horse is out of the barn. The question is, can we get it back in? And if we don't get it back in, what kind of wagon it's going to be dragging with us in the years ahead. And I think it's up to the United States to lead. I think it's up to the United States to lead for ourselves and in the international community with approaches of this nature. And I don't know any other approach other than payment mechanism approaches that are effective on enforcement and that can be replicated easier in other countries in the world. And that is why to me it is so important.

Beyond that, I don't have any questions for this panel, because this panel has been so forthcoming and direct and thoughtful in their presentations to the subcommittee. And I want to thank you very much, Madam Chairwoman.

Chairwoman KELLY. I thank you, Mr. Leach.

There are obviously no more questions for this panel, and I really thank you for your indulgence for the long wait that we had. It was unexpected. Since there are no more questions for the panel, the

Chair notes that some Members may have additional questions, and they may wish to submit those in writing. Without objection, the hearing record is going to remain open for 30 days for Members to submit written questions and witnesses to place their responses in the record.

Oh, Mr. Goodlatte, you just got here? Do you have—all right. Thank you.

I want to again thank this panel for their time and patience with us. The first panel is excused with the Subcommittee's grateful, grateful gratitude. And we are going to take just a quick break so that we can have the second panel take their seats. Thank you all very much.

[Recess.]

Chairwoman KELLY. For our second panel, we are very grateful that Mr. Bill Saum could join us. He is the Director of Agent Gambling and Amateurism Activities for the National Collegiate Athletic Association. He is going to discuss the effect of internet gambling on amateur sports, the integrity of the games, and the athletes.

Next we are going to hear from Mr. Mark MacCarthy, the Senior Vice President of Public Policy for Visa U.S.A., Incorporated, who will discuss the challenges to the credit card industry with internet gambling and the accompanying credit card use.

Then we are going to hear from Ms. Sue Schneider. She is the Chairman of the Interactive Gaming Council, which represents manufacturers and licensers of software used to enable internet gambling to function.

Then we are going to have Ms. Penny Kyle, the Executive Director of the Virginia Lottery and the President of the National Association of State and Provincial Lotteries. She will share with us the perspective of the State lotteries.

And finally, we will hear from Mr. Greg Avioli, the Deputy Commissioner of the National Thoroughbred Racing Association, who will share with us the perspectives of the horseracing industry.

I want to thank all of you for taking time out of your schedules to be here with us today and to share your thoughts with us, and I certainly do thank you for your patience in waiting to appear on this panel. Let us begin with you, Mr. Saum.

STATEMENT OF BILL SAUM, DIRECTOR, AGENT GAMBLING AND AMATEURISM ACTIVITIES, NATIONAL COLLEGIATE ATHLETIC ASSOCIATION

Mr. SAUM. Madam Chairwoman and Members of the Subcommittee, thank you for the opportunity to testify on behalf of the National Collegiate Athletic Association and to share with you our concerns related to the growth and impact of sports gambling on the internet.

The NCAA is a membership organization consisting of nearly 1,000 universities and colleges and is devoted to the regulation and promotion of intercollegiate athletics for over 300,000 male and female student-athletes.

Though the growth of internet gambling has seemingly sprouted overnight, this is not a new issue for the NCAA. For the past 4 years, we have worked with House and Senate sponsors in an ef-

fort to adopt legislation that would in part ensure that all sports gambling on the internet is prohibited in this country. Why? The answer is quite simple. When people place wagers on college games, there is always the potential that the integrity of the context may be jeopardized and the welfare of the student-athletes may be threatened. For example, many of you are aware of the recent point-shaving scandals on the campuses of Northwestern University and Arizona State University. While these cases occurred before the rise of the internet gambling industry, the impact of these sports gambling incidents must not be minimized. Many, many dollars were wagered on these games. The result? Several of the student-athletes involved were indicted and sentenced to time in a Federal prison. Coaches and teammates were betrayed, and the two schools have seen their reputations tarnished. It is clear that sports gambling is not a victimless crime and that the potential for similar incidents to occur has increased now that sports bets can be placed on the internet.

Perhaps the most frustrating aspect of internet gambling is that while we all acknowledge the wondrous benefits of the internet age, it also has presented some significant challenges. Today this new communications medium, the internet, allows online gambling operators to circumvent existing U.S. laws aimed at prohibiting sports gambling. This is why we believe that new Federal legislation is needed to address the rapidly transforming world of gambling in cyberspace.

As you listen today to witnesses arguing the pros and cons of internet gambling, please do not overlook the potentially harmful impact of this activity on young people. A growing consensus of research reveals that the rates of pathological and problem gambling among college students are three times higher than the adult population. This fact surely did not go unnoticed when the National Gambling Impact Study Commission recommended a Federal ban on internet gambling in June of 1999.

Just 4 years ago, when the NCAA became involved in the legislative effort to ban internet gambling, there were only four dozen internet gambling sites. Now there are 1,4000 unique internet gambling websites. Today college students are perhaps the most wired group of individuals in the United States. They can surf the web in their school library, in the computer lab, or in the privacy of their dorm room. The emergence of internet gambling enables students to wager behind closed doors, anonymously, and with the guarantee of privacy. Furthermore, the ease and accessibility of internet sports gambling creates the potential for student-athletes to place wagers over the internet and then attempt to influence the outcome of the contest while participating on the court or playing field.

If left unchecked, the growth of internet gambling could be fueled by college students. Today college students are armed with the means to gamble on the internet. A year 2000 study by Nellie Mae indicates that 78 percent of college students have credit cards. Thirty-two percent have four or more, and that the average debt for these undergraduates is approximately $2,750 per card.

In my position as the NCAA Director of Agent, Gambling and Amateurism Activities, I have seen how students are falling victim

to the lure of internet sports gambling. Offshore operators continue to implement aggressive marketing tactics. There are billboards promoting internet gambling sites across the country. Student-athletes continue to complain about receiving unsolicited e-mails for sports gambling websites. And there have been reports of individuals passing out flyers touting internet gambling opportunities at fraternity houses.

I have spoken with students who have lost thousands of dollars on the internet. In fact, last year at a congressional hearing, we played a videotape account of a college student who in just 3 months lost $10,000 gambling over the internet. Please be assured that this is not a unique experience. We have heard from others with similar stories.

Finally, our staff is beginning to process NCAA rule violation cases involving internet sports gambling. On the legislative front, the past four years have been marked by frustration. Those supporting efforts to adopt the legislation have come very close to achieving their goal, but in the end have been thwarted by aggressive and well-financed opposition. The real challenge in crafting legislation——

Chairwoman KELLY. Mr. Saum, you have run out of time. Can you summarize, please?

Mr. SAUM. Yes. The real challenge in crafting legislation that will not only address the problems associated with internet gambling but also provide an effective enforcement mechanism will have an impact on these offshore operations. The NCAA urges the Subcommittee and Congress to not let this opportunity slip away, and thoughtful legislation may be successful in significantly curtailing this growth and popularity of internet gambling in this country. Thank you.

[The prepared statement of Bill Saum can be found on page 146 in the appendix.]

Chairwoman KELLY. Thank you very much.

Mr. MacCarthy.

STATEMENT OF MARK MacCARTHY, SENIOR VICE PRESIDENT PUBLIC POLICY, VISA U.S.A. INC.

Mr. MACCARTHY. Thank you, Chairwoman Kelly and Members of the Subcommittee.

The Visa Payment System is the largest consumer payment system in the world. The over one billion Visa cards issued by our 21,000 members are accepted at over 20 million locations.

Chairwoman KELLY. Mr. MacCarthy, can you pull that microphone a little more closely to you, please?

Mr. MACCARTHY. Is that better?

Chairwoman KELLY. Thank you. Much better.

Mr. MACCARTHY. The over one billion Visa cards issued by our 21,000 members are accepted at over 20 million locations to buy over $1.8 trillion worth of goods and services every year. In the U.S. alone, cardholders use Visa cards to buy over $90 billion worth of goods and services.

Visa recognizes that internet gambling can raise important social issues, especially access by problem and underage gamblers. Also, while internet gambling represents only a negligible part of our

total transactions, it imposes disproportionate legal and operating risks for Visa and for its members.

So Visa has taken steps to address internet gambling. Visa card issuers must advise cardholders that internet gambling may be illegal in their jurisdiction and that Visa cards should only be used for legal transactions.

Visa also cooperates with law enforcement agencies in their efforts to prosecute illegal domestic internet gambling operations. And Visa has taken steps to enable card issuers to block potentially illegal internet gambling transactions.

Visa requires internet gaming merchants to use a combination of codes that tells the card issuer that a transaction is likely to be an internet gambling transaction, and this allows a card issuer to deny authorization for these transactions. The sheer volume of transactions that Visa handles requires it to rely on this merchant code. The Visa operating system operates at a pace of 35.5 billion transactions per year. Visa processes an average of 2,500 messages per second and has a peak capacity of 4,000 messages per second.

Our coding system has limitations. For it to work, merchants must accurately code transactions. Visa merchants are required to properly code, and there are penalties for failures to do so, but there are obvious incentives for unscrupulous internet gambling merchants, to try to hide from Visa and from its members.

Coding only informs card issuers that the transaction is likely an internet gambling transaction. It does not tell us whether the transaction is illegal. For example, U.S. cardholders visit foreign countries where internet gambling is authorized and where the use of credit cards to pay for online gambling is entirely legal. Online gamblers often use electronic cash for auctions, online purchases or for internet gambling. The coding system that Visa uses would not capture these transactions as internet gambling transactions.

We believe that partly as a result of these efforts, these alternative forms of payment are becoming a payment system of choice for internet gambling. I was pleased to notice that other witnesses have made this same point in their testimony.

Under current law, it is impossible to determine quickly and efficiently whether a particular internet gambling transaction is illegal. Part of the problem is ascertaining exactly where a cardholder originates the transaction.

Going forward, we believe that the responsibility for illegal acts should be placed squarely on the shoulders of the illegal actors themselves—the gamblers and the casinos that engage in illegal gambling operations. Making payment systems responsible for policing internet gambling does not provide a practical and effective solution for this complex social problem. And it is hard for us to see how Congress can address payment systems and internet gambling without clarifying the underlying legal landscape. A law that makes all internet gambling illegal would be hard for us to enforce and would raise significant cross-border jurisdictional issues.

But the fundamental point is that if policymakers declare internet gambling illegal, unscrupulous merchants will simply stop coding their transactions accurately, and we will have no way of knowing which transactions are internet gambling ones. Conversely, a more complex law that allows for multiple exceptions for a ban on

internet gambling, such as allowing internet gambling on an intrastate basis or permitting certain types of gambling, such as pari-mutuel betting, would be impossible for us to enforce. No coding system could possibly reflect all these variations.

Thank you for the opportunity to testify before you today, and I would be happy to answer any questions.

[The prepared statement of Mark MacCarthy can be found on page 155 in the appendix.]

Chairwoman KELLY. Thank you very much, Mr. MacCarthy. You have certainly given us some food for thought.

Ms. Schneider.

STATEMENT OF SUE SCHNEIDER, CHAIRMAN, INTERACTIVE GAMING COUNCIL

Ms. SCHNEIDER. Madam Chairwoman and Members of the subcommittee, I have served as the Chairman of Interactive Gaming Council since its formation in 1996, and I would like to applaud you for holding this hearing to learn more about this very complex subject and to really educate yourselves about the public policy issues that are opened here. It is a situation where it is very complex. It is international in nature and can be very complicated.

The IGC itself is a not-for-profit trade association with over 100 member companies from around the world. These are companies that are operators, software suppliers, e-commerce providers, or like my own company, we provide information services.

The mission of the organization is to provide a forum for what we consider to be the legitimate participants in the industry to work toward uniform standards for those participants on an intergovernmental basis and to provide a unified voice to advocate for the interests of both the members and the consumers who enjoy our services.

I have included in the appendix some things that I think you might find of interest: A Code of Conduct, Responsible Gaming Guidelines, and most recently, a Seal of Approval program that has been adopted by the IGC, and members are beginning to participate in that.

We feel that neither governments nor consumers will tolerate an industry that doesn't extend adequate protections to its consumers, and I think that's something where we agree with policymakers, is how do you extend those protections? I can tell you from having worked with an information publication that was consumer-oriented, consumers are concerned about two things: Are the games fair? Is their betting fair, and will they get paid? And those are the common things that they are most concerned about. And it is something that again takes international exposure and cooperation here.

What we are not are an association of members who set up shop, take off with the dollars and run. And quite frankly, there have been very few instances of that in an industry that's been having the kind of growth that has existed over the last few years.

We are also not unaware of and not insensitive to the issues of underage or problem gambling. And quite frankly, some of the technology that exists allows for the kind of tracking of that, particularly when it comes to some of the issues of compulsive gambling, loss limits, self-exclusionary type of things, a variety of

things like that, which we can get into more in the question-and-answer session if you would like to learn more about that.

As we mentioned, there are at least 54 jurisdictions around the world that offer sanctioned internet gambling in some way, and we have included that list in there also. Countries such as Great Britain and South Africa are now exploring regulatory structures. And again, we work with the international body of gaming regulators to look at baseline standards so that there is some consistency there.

As you are likely aware, Nevada, for example, and even New Jersey have had legislation introduced, and Nevada passed to allow for regulatory structure if they can be guaranteed that certain controls are in place.

I have added some information on the size of the industry and again, I think Sebastian covered that quite a bit, so I'll move by that.

But I do want to say again to reiterate that the demand is within the U.S. in terms of the market for these services. And I think what that does is really make the public policy issues even more of a challenge. But among those, we feel that both the State versus Federal oversight, those tensions on who does have oversight of this, is something that needs to be openly discussed. Looking at the location of where the gambling transaction takes place and the jurisdictional issues there, and again, trying to get some harmonization of regulations.

I think the whole issue of the financial transactions is something that we have to look at very carefully. Do you want to be a chokepoint and really put out to the international world that that sort of thing happens. I know there's a lot of inconsistencies to a certain extent when you look at like the French Yahoo case that some of you may be familiar with. Some of those kind of issues, you get into that interplay of trying to control a medium that has been set up to not be controlled. And those are the kind of concerns that I think are of essence as you look at using financial transactions as a control point.

And as you have also heard, that the whole issue of coming up with more anonymous e-cash services as a result of those kind of restrictions are something that will probably be a reality there.

I do want to mention that there are two things that I would ask that you keep in mind. One, as we've mentioned before, the Volstead Act, and trying to curb demand in that regard when you have some people, a number of people in America that are looking at that as an opportunity for an entertainment that they want to take advantage of. And I think the other thing to look at is how Las Vegas has evolved. It started out, you know, you talk about the Wild West. That was the Wild West there, and it has now evolved through a regulatory structure that has been I think a benefit to consumers, and that's what we want to advocate for.

Thank you very much.

[The prepared statement of Sue Schneider can be found on page 169 in the appendix.]

Chairwoman KELLY. Thank you very much, Ms. Schneider. I apologize for cutting you off and cutting you short on your testimony, but you know your written testimony is already a part of the record, and we will be asking questions.

Ms. Kyle.

STATEMENT OF PENELOPE W. KYLE, EXECUTIVE DIRECTOR, VIRGINIA LOTTERY; PRESIDENT, NATIONAL ASSOCIATION OF STATE AND PROVINCIAL LOTTERIES

Ms. KYLE. Good afternoon, Madam Chairwoman, Congressman Leach and Congressman Goodlatte. My name is Penny Kyle, and I am serving this year as the President of the North American Association of State and Provincial Lotteries. This is the group that represents every U.S. lottery, of which there are now 39; the six provincial lotteries of Canada, the National Lottery of Mexico, and the lotteries in the Virgin Islands, Puerto Rico, and Jamaica.

I am here today, first of all, to tell you that the 39 U.S. lottery directors actively support what this subcommittee is trying to do. We think that the issue of addressing illegal and unregulated internet wagering needs to be undertaken, and we applaud your efforts.

As State lottery directors, our members operate under some of the most stringent legal and security standards in the world. And we do this because as State governments, we believe it is in our best interest if we are to maintain the high level of public trust that we currently have with our citizens in our various jurisdictions.

Therefore, your efforts to outlaw illegal internet operations are welcomed and supported by those of us who currently adhere to the legal wagering rules.

It should be noted that this organization has not taken a for or against position regarding the sale of lottery tickets on the internet. We feel this is a position that must be taken by each of the individual States to determine the forms of regulating its own gaming as well as the methods that are offered in that State.

My goal in appearing before your subcommittee today is to make one key point to you. That is that NASPL cannot support any internet legislation that would preempt the right of the Nation's governors and State legislators to either prohibit, authorize, or regulate gaming within their own borders.

Since the inception of the first modern lottery in New Hampshire in 1964, State meeting governments have had the right to authorize and regulate their State lotteries. They write billions of dollars for good causes, such as education, the environment, and senior citizen programs.

We stand by the statement made by the National Governors' Association, and I quote as follows:

"States possess the authority to regulate gambling within their own borders and must continue to be allowed to do so. An incursion into this area with respect to on-line gambling would establish a dangerous precedent with respect to gambling in general as well as broader principles of State sovereignty."

It should be noted that there are several State lottery members of NASPL who are opposed to offering State lottery products over the internet. These States feel very strongly about this issue and would oppose any attempt to authorize any such games.

On the other hand, there are some NASPL State lottery members who feel that there may come a time in the future when it is appropriate to offer such games. I make this point, Madame Chair-

woman, to illustrate an important common theme among our membership. All of us may not agree on the value or the appropriateness of offering lottery products on the internet, but we are united in the belief that it is clearly each State's right to authorize and regulate its own lottery and the methods of selling its own lottery products.

In conclusion, I would ask that this subcommittee and other relevant congressional committees, while addressing the issue of illegal and unregulated internet gaming, please respect the historical right of States to authorize and regulate gaming within their own boundaries.

I thank you again for allowing me to represent the views of the North American Lottery Industry.

[The prepared statement of Penelope W. Kyle can be found on page 185 in the appendix.]

Chairwoman KELLY. Thank you very much, Ms. Kyle.

Mr. Avioli.

STATEMENT OF GREGORY C. AVIOLI, DEPUTY COMMISSIONER, NATIONAL THOROUGHBRED RACING ASSOCIATION

Mr. AVIOLI. Thank you, Madame Chair.

I'm testifying today on behalf of the National Thoroughbred Racing Association which is the national organizing body for the sport of thoroughbred racing, which represents the interests of racetracks, owners, and breeders. Horseracing and breeding in the United States is a major agri-business. It currently employs nearly 500,000 full time employees and has an annual economic impact of over $34 billion on the U.S. economy.

Wagering on horseracing is permitted in 43 States and generates over $500 million each year in State and local taxes. Racing is also a very popular spectator sport, with over 30 million fans coming to the races last year and that's second only to major league baseball.

Prior to 1970, wagering was only available to patrons who were live at the racetrack. In 1970, the New York Legislature authorized off-track wagering. Since that time, all 43 racing States have authorized the tracks in those States to send pictures of their races to other States. That's a process known as simulcasting.

As part of the growth of simulcasting, racing improved its product by starting a process known as "common pooling" where they would combine many betting pools in one or more jurisdictions. This process uses sophisticated computer networks and now relies heavily on the internet to transmit the information.

Another technological advance for racing over the last few decades was the development of advanced deposit or account wagering where a person can set up an account with a licensed facility and then wager from another location. Currently, 11 States have authorized this account wagering.

I bring this up because racing's use of modern technology I've just described has allowed the racing industry, and the $34 billion agri-business it supports, to survive in a very competitive gaming environment.

As a statistic, about 50 years ago, racing had 100 percent of the legal gaming market in the United States. As we sit here today, it's less than 5 percent. Throughout history, the prohibition or le-

galization and regulation of gaming has been primarily left to the States and not to the Federal Government. In this regard, wagering has been regulated on the State level for 75 years.

In 1978, the State regulation of horseracing was supplemented by the Federal Government in a very specific way with the passage of the Interstate Horseracing Act of 1978. In that Act, Congress stated in its congressional findings that it is the policy of Congress to regulate interstate commerce with respect to wagering on horseracing in order to further the horseracing and legal off-track betting industries in the United States.

Just last year, Congress amended the Interstate Horseracing Act to clarify that interstate simulcasting and account wagering can be conducted via telephone or other electronic means which would include the internet where lawful in the States involved. This was just in the last Congress.

Again, similar to the other speakers you've heard today, our industry feels very strongly that the regulation of all forms of gaming is essential to protect the public and assure compliance with applicable laws. We are adamantly opposed to any unregulated gambling whether via the internet or any other medium.

In the last decade, the internet has been used by offshore unregulated entities who have pirated money from licensed racetracks in the United States. These operations are able to offer more attractive betting propositions because they don't pay U.S. taxes and they don't pay the revenue shares that currently go back to support racing and purses in this country.

It's been estimated that this year, as much as $750 million of what otherwise would be a total of $15 billion will be wagered offshore. That is a $750 million gaming loss to the licensed industry in the United States.

In light of the posed threat to our industry from internet gambling, we have supported a number of congressional initiatives in the last few years to curb illegal internet gambling. We've worked closely with Congressman Goodlatte last year. As a result of participating in the legislative process, however, we are aware that any legislation dealing with this issue will have very technical legal issues, and we are concerned that imprecisely or improperly drafted legislation could have an unintended effect.

For example, some legislation last year, without intending it, would have outlawed the legal business of simulcasting, which had nothing to do with the internet, but because computers that were included in the definition of the internet are used in simulcasting, that bill would have, on its face, outlawed the core business that we have today.

That's a good ending point.

[Laughter.]

[The prepared statement of Gregory C. Avioli can be found on page 190 in the appendix.]

Chairwoman KELLY. Thank you very much.

I'm going to ask one question very quickly.

I would like to ask Mr. Saum about whether or not you are aware of a study that was done by the student journalists at Santa Clara University that came up with numerous instances of stu-

dents racking up huge credit debts gambling. Some of this apparently was done on the internet.

I have here a story that the students wrote, and I'm going to request that it be made a part of the hearing record.

[The information referred to can be found on page 41 in the appendix.]

Chairwoman KELLY. Are you aware of this and would you like to elaborate on that?

Mr. SAUM. Yes, ma'am, we are aware of it. We've been in communication with a few of the authors of this article, and it's fascinating from the stance that they actually began as a report for one of their classes, they began by sharing some of their own stories, and then they went out and started interviewing other students in the Silicon Valley area. From one student, they expanded it to other students, and the stories that they heard were rather alarming. They heard the stories of the easy access to the internet, the easy access using their credit cards. When they maxed out their credit cards, they were given new credit cards and from there the debt rose to the level of thousands of dollars. And several of the kids were in the tens of thousands of dollars area.

Chairwoman KELLY. Thank you very much.

I want to know, I have one other question here. Mr. Suarez indicated—and this is a question for Ms. Schneider—Mr. Suarez indicated that 15- and 17-year olds were able to access offshore internet gambling sites during an investigation that they conducted. Yet, I see that one of the items in your Code of Conduct says that members will institute controls that require customers to affirm that they are of lawful age in their jurisdiction, and that they will institute reasonable measures to corroborate that information. It sounds like some of the offshore sites are not complying with your code.

My question really is whether or not there is any way to design software in such a way that you're going to be able to exclude money laundering and kids from using the site. These people who are non-compliant, are they members of your IGC?

Ms. SCHNEIDER. The three they had targeted are not members. This is the problem with a voluntary trade association, quite frankly, is you can't get 100 percent of the people in. That's why regulation is an optimal solution in that regard.

In terms of what you can do in terms of underage gambling, what a number of operators do is go through kind of a vetting process. When you open an account, they can require and do require copies of passports or birth certificates or that sort of thing, to be able to get a sense of documentation of the age of that particular player.

Down the road, there are things coming now in terms of biometric encryption tools to make sure that the person that established the account is indeed the person that's playing. So you do have a situation there where there are technological tools that are being developed now that will assist with that.

Mr. LEACH. [Presiding] Thank you very much.

Mr. Goodlatte, do you have any questions?

Mr. GOODLATTE. Thank you, Mr. Chairman.

Ms. Schneider, let me follow up on that question. Are you saying that everyone of your 100-member organizations presently requires submission of some kind of documentation, like passports or birth certificates, before they will allow anybody to obtain membership or whatever you require, each one of those organizations requires to bet on-line?

Ms. SCHNEIDER. I'm not saying that. Number one, not a hundred of the members are all operators.

Mr. GOODLATTE. Of the ones that are operators.

Ms. SCHNEIDER. I can't say with any certainty. I think you have the same problem in the hearing that came up last year with the racing industry in terms of whether they were all compliant with taking wagers only from those 8 States.

When you have a volunteer association, you can't do it. It's something we would hope for.

Mr. GOODLATTE. Have you checked on that?

Ms. SCHNEIDER. Have we checked on it? We know that the leading ones that do a big volume do have those kind of controls in place.

Mr. GOODLATTE. If you are capable of doing that to screen out people who are minors, you would similarly, from the same information provided to you, have the ability to screen out people who are placing those bets from the United States or who are United States citizens.

Do any of those organizations do that? Do any of them attempt to not engage in illegal gaming in the United States which I think virtually every legal scholar that I'm aware of believes it is illegal to do in the United States under the current law, to say nothing of any law we might introduce now.

Under current law, I know some individuals have been prosecuted for that very violation. Do any one of the members of your organization screen out United States citizens because they know that it's against the law to engage in that activity in the United States?

Ms. SCHNEIDER. Of the operators that are out there, they each take into account, from their legal counsel, who'll they'll take play from. Yes, we do have some that won't take any play from the U.S. We have some that take play from the U.S. We have some that take play from the U.S. States that have passed explicit laws that prohibit internet gambling, so it's a company-by-company decision in terms of how they handle that.

Mr. GOODLATTE. Whether or not they break the law?

Ms. SCHNEIDER. Sir, with all due respect, if the law was that clear, and there is case law that says otherwise in some of the jurisdictions, I don't think we would be here having these discussions if it was that crystal clear. It's clearly an area that's still in need of clarification.

Mr. GOODLATTE. Let me ask you this. Would your organization exclude from membership those organizations who violated the law if there were a new law that was passed that said very clearly that you cannot engage in this activity on the internet with those who are placing these bets from the United States?

Ms. SCHNEIDER. That's a process that we would have to go through in terms of making that kind of clarification. Again, these

are international companies that are operating, you know, for all the talk about it's an unregulated environment, I have a feeling that your colleagues in some States in Australia would take umbrage at that, because it is a highly regulated jurisdiction there.

So you get into those kind of multi-jurisdictional concerns that I addressed before. That's the biggest challenge with this. And I think we have to be forthcoming.

Mr. GOODLATTE. The law is very clear in the United States, one of the two parties to it. It's against the law in the United States. That is the issue that concerns Ms. Kyle sitting next to you, your member organizations are without paying any U.S. taxes, without complying with any kind of regulatory scheme, as the gentleman from New Jersey Gaming Commission testified, in violation of the laws of the United States as they exist right now.

We do need to beef up those laws. We do need to make them even clearer than they are now. We do need to give law enforcement new remedies to deal with the problem.

But the fact of the matter is whether there are different laws in other countries, or around the world, the law in the United States is that you can't do this. Nonetheless, organizations that are members of your trade association are engaged in that activity.

Let me ask Mr. MacCarthy a question.

When you have folks who fraudulently or falsely code their credit card information, what do you do when you find one that's brought to your attention?

Mr. MACCARTHY. We have a general rule that our merchants must properly code the transactions.

Mr. GOODLATTE. If a merchant doesn't properly code, what do you do?

Mr. MACCARTHY. If it's brought to our attention, we have a process whereby we investigate, we tell the bank that works directly with the merchant about the problem, and we instruct that bank to take steps to correct it, to instruct the merchant in the process of correctly coding. If that doesn't work, then there's a process of fines. And if the infraction persists over an indefinite period of time—the exact number of months is not prescribed—then we have the capacity to separate that merchant from the system.

Mr. GOODLATTE. Wouldn't you have the same capacity to do that for merchants who engaged in the activity I just described with relation to members of Ms. Schneider's organization and others that are offering these services that are doing so illegally in the United States?

Mr. MACCARTHY. If the circumstance you are describing is an offshore internet gambling merchant who improperly codes his transactions, does not use the code for gaming, does not use the code for electronic commerce, and puts transactions into our system that potentially put our issuers at risk for business expenses and for legal expenses and other risks, we would take steps to try to make sure that that merchant properly coded and put the transactions into our system in a fashion that allowed our member issuers to block those transactions if they so decided.

Mr. GOODLATTE. If Mr. Suarez, the Director of the Division of Gaming Enforcement in New Jersey, presented evidence to you that his investigators had found that a company in Antigua or any

of a host of other countries around the world were offering gaming services in New Jersey, and they got under a hypothetical law, a law that I hope Mr. Leach will be able to pursue in the law in the near future, but if they were to bring you a court order that said that they were engaged in that activity in New Jersey or Virginia or any other of the 50 States that banned this activity or just under Federal law, you would be able to take steps to cut them off from the use of Visa cards.

Mr. MACCARTHY. Let me go back and reconstruct the example, if I may. If it's an internet gambling operation and it's actually operating in New Jersey or in Virginia.

Mr. GOODLATTE. Let's say it's in Antigua and the bettor is in New Jersey. Suarez, as an investigator, happens to be doing an undercover operation.

Mr. MACCARTHY. Let's start with a U.S. example. If that were the case, because operating an internet gambling operation in New Jersey or Virginia, or in almost all the States except perhaps Nevada, since that is illegal, we would take steps immediately working through the merchant's bank to cut that internet gambling merchant off from our payment system and we would inform law enforcement officers right away. We do that under current law. We work very cooperatively with law enforcement people in that area.

And the other circumstance that you described, where law enforcement officials or any other people brought to our attention the fact that a particular offshore internet gambling merchant was improperly coding the transactions and expressed the view that that was contrary to U.S. law, we would work cooperatively with the law enforcement entity. We would immediately instruct the merchant bank to take steps to ensure that that internet gambling merchant properly coded the transactions.

Mr. GOODLATTE. In other words, what we are attempting to accomplish could be accomplished.

Mr. MACCARTHY. If the internet gambling merchant then continued to insert into the stream of transactions all and only properly coded transactions, then we would accomplish the objective of giving our people the capacity to block those kind of transactions if they so choose. That's under current law.

If the internet gambling operation decided, instead of cooperation with us and law enforcement entities, decided that they would simply stop processing transactions in any fashion and vanished entirely from our system, we would have no way of knowing where they might resurface, and so it would be very difficult to follow them.

But insofar as they maintain the contact with our acquiring merchant, we would be able to work with them to make sure that they properly coded.

Mr. GOODLATTE. I assume these organizations have a desire to live off of the trade name they develop and therefore to just disappear and resurface poses some problems for them, especially if they're going to continue to use a legitimate means of collecting funds like Visa or another legitimate business institution.

Thank you, Mr. Chairman. I've abused my amount of time here.

Mr. LEACH. Thank you very much, Mr. Goodlatte. We are all very appreciative of what you've been attempting to do.

We do have a problem with votes on the floor. This is a very complicated day and very complicated legislation. In fact, it's so complicated, we are apparently tied up in process knots.

But I want to thank this panel very much. Let me say, procedurally, that all of your full statements will be placed in the record without objection.

Without objection, Members will have 30 days to submit written questions and responses if that's possible from the panels.

I just personally would like to say we would also be very appreciative of any precision and recommendations of changes to legislation that may be offered by Members of the subcommittee that you become aware of.

Certainly, approaches of Mr. Goodlatte, I hope that you feel free to talk with Bob about and those pieces of legislation that may be offered in this panel, most particularly HR 556, but I think there may be others as well.

With that, let me say we are very appreciative of your coming before us and we thank you for your time and your effort and we hope it will continue.

Thank you very much. The hearing is adjourned.

[Whereupon, at 5:20 p.m., the hearing was adjourned.]

A P P E N D I X

July 12, 2001

STATEMENT OF REP. SUE KELLY CHAIRWOMAN, SUBCOMMITTEE ON OVERSIGHT & INVESTIGATIONS HEARING ON THE FINANCIAL ASPECTS OF INTERNET GAMING: GOOD GAMBLE OR BAD BET?

July 12, 2001; 2:00 p.m.; 2128 Rayburn

We convene here today to listen to testimony from two panels of distinguished witnesses about a timely, but controversial, topic: gambling on the Internet.

In a few short years, the Internet gambling industry has exploded. According to an Internet gambling committee of the National Association of Attorneys General, there were less than 25 such sites on the Web in the mid-1990s. Today, Bear Stearns, one of the nation's leading securities firms, estimates that there are between 1,200 and 1,400 e-gaming Web sites. Bear Stearns projects that as the industry continues to grow, such Internet sites could generate an estimated $5 billion in revenues by 2003. That figure approximates roughly half of last year's casino earnings in the State of Nevada.

Internet gambling presents a complex set of legal, financial, technical, and social challenges. On the legal front, it is believed that most forms of interstate Internet gambling are prohibited by Federal law under the Interstate Wire Act in Section 1084 of Title 18 of the U.S. Code. For years, authorities have used the Wire Act to combat illegal betting by phone or other wire communications. Now, with the advent of Internet technology, the Wire Act and other related provisions of Federal law also stand as a legal obstacle against the establishment of Internet casinos on U.S. soil.

State laws have similarly banned Internet gambling operations, and we will hear today from New Jersey's Director of Gaming Enforcement about that State's efforts to sue offshore casinos to prevent them from operating within New Jersey's borders. However, some State laws against Internet gambling may be about to change if the legislation enacted in Nevada last month is any indication.

The most serious offenders in the Internet gambling arena are the virtual casinos operating offshore, beyond the reach of U.S. law. One estimate puts the number of foreign jurisdictions authorizing or tolerating Internet gambling at fifty. This includes not just the well-known bank secrecy jurisdictions of the Caribbean but other countries like Australia. The lure of lucrative licensing fees and the possibility of sharing in gambling receipts are proving to be powerful incentives to enter the Internet gambling business. Antigua and Barbuda have reportedly licensed more than 80 Internet gaming Web sites already, charging a $75,000-$85,000 licensing fee for a sports betting site and $100,000 for a virtual casino. A report prepared for the South African government, as reported in the Bear Stearns study, revealed that Internet gaming revenues could yield up to $140 million in foreign exchange.

While Internet gambling represents a jackpot for such foreign jurisdictions, it is a wheel of misfortune for far too many Americans who struggle with gambling addictions and the loss of jobs, wrecked marriages, and destroyed finances that often follow. With a click of a computer mouse, any American armed with a credit card can have instant, anonymous access to round-the-clock gambling from the privacy of their homes. Students on college campuses – with nearly unchecked access to credit cards issued by eager credit card companies – have already been known to rack up large gambling debts. As we will hear today, all of the social hazards associated with problem gambling at brick-and-mortar sites are of equal, if not greater, concern when it comes to on-line gambling.

Furthermore, Internet gambling poses a serious problem to our youth. In the areas in which gambling is legal, strict laws have been enacted to ensure our children are prohibited from participating. In many homes the children are far more computer literate than the parents, what possibly would stop a child from placing a bet with their parent's credit card? Since our society has made a conscious decision to keep children from this activity we must take steps to ensure that online casinos do not victimize our children. The issue of what can we do to protect children from these sites will be one of my first questions for our panelists today.

In addition to the social problems associated with Internet gambling, U.S. authorities warn that Internet gaming offers a powerful vehicle for laundering funds from illicit sources as well as to evade taxes. A 2000-2001 Financial Action Task Force (FATF) report on money laundering typologies indicates that there is evidence in some FATF jurisdictions that criminals are using the Internet gambling industry to commit crime and to launder the proceeds thereof. The use of credit cards and the placement of sites offshore make locating the relevant parties, gathering the necessary evidence, and prosecuting those parties difficult if not impossible.

Despite the many problems associated with Internet gambling, there is clearly money to be made in this business, and U.S. firms are increasingly eager to claim their share. As we will hear today, U.S. credit card companies, software firms, public relations and advertising companies, and other U.S.-based enterprises are already knee-deep in the Internet gambling business. Within the last year, two U.S. companies – MGM Mirage and Harrah's – have announced new on-line play-for-free or play-for-prizes operations that are but a short step away from actual Internet gambling. In addition, as noted earlier, Nevada recently became the first state in the nation to enact legislation to open the door to Internet gambling. How that law will survive a challenge under Federal law remains to be seen. Nevertheless, it is clear that absent strong Congressional action, the United States may be poised itself to head down the slippery slope of Internet gambling.

In 1999, the Congressionally-mandated National Gambling Impact Study Commission unanimously recommended a Federal ban on Internet gambling. Testifying at a hearing before the Banking Committee last Congress, Commission Member Richard Leone explained that unlike the regulatory regimes that have accompanied the expansion of other forms of gambling in the United States, the emergence of Internet gambling has occurred with no regulatory structure. As a result, the current framework of Federal and State laws governing gambling can be easily circumvented. The Commission noted that the problems associated with Internet gambling include: (1) the potential for abuse by gambling operators who can alter, move, or entirely remove sites within minutes; (2) the ability of gambling operators or computer hackers to tamper with gambling software to manipulate games to their benefit; and 3) the provision of additional means for individuals to launder money derived from criminal activities.

The Commission concluded that because Internet gambling crossed state lines, it would be difficult for States to effectively control it and that Federal legislation was the only recourse. The Commission further rejected the argument that Internet gambling could be effectively regulated, and recommended, instead, a ban on any Internet gambling not already authorized by law, and without new or expanded exemptions. Although the States do not normally welcome Federal legislation on such matters, the National Association of Attorneys General, speaking on behalf of State Attorneys General, has indicated strong support for Federal action.

In response to the Commission's recommendations and testimony from other interested parties, the House Banking Committee approved legislation last year that would have tackled the problem of Internet gambling by prohibiting gambling operations from accepting credit cards, checks, or other bank instruments in connection with illegal Internet gambling. The Judiciary Committee also addressed the legal aspects of Internet gambling under separate legislation, but the 106th Congress adjourned before meaningful Internet gambling legislation could be enacted. I fear now that such failure is being misinterpreted as a green light to those in U.S. industry who are interested in launching on-line gambling operations of one type or another.

In closing, let me say that the purpose of the hearing today is one of oversight. It will help us assess what has happened in the Internet gambling arena since Congress examined the issue last year. It is my intent, however, not to stop at oversight, but to work with the legislative Subcommittees under this Committee to support appropriate legislative action in the months ahead. This issue can no longer simply be left to random events and foreign jurisdictions. It is time for Congress to address these issues and identify an appropriate public policy response.

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STORY BY
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After putting the finishing touches on his Economics homework, "Justin," a Saint Mary's senior, picks up the phone and dials a familiar number. "Are you playin'?" he asks. The ritual begins. He dresses quickly in the dark, careful not to wake his roommate, and splashes his face with cold water. Thirty minutes later, a cigarette dangles between two fingers and a computer screen glows in the dark of his friend's door room. Justin paces behind his friend's desk -- another long night of Internet gambling has begun. A fan pushes the stale air around the room as they plot their next move. They draw their cards and the garish letters of "ParadisePoker.com" flash underneath the full house on the screen. They've won this hand, but the $20,000 Justin has poured into his gambling habit colors the victory.

But while Justin seems in over his head, for he and other Bay Area college students, it could be even worse. Problem gamblers between 18 and 25 lose an average of $30,000 each year and rack up $20,000 to $25,000 in credit card debt, according to the California Council on Problem Gambling. And according to a January health advisory issued by the American Psychiatric Association, 10 to 15 percent of young people reported having experienced one or more significant problems relating to gambling.

Still, despite the area's proximity to Tahoe and Internet-savvy youth population, people are ignoring the problem. Many Bay Area university conduct codes do not even mention gambling while local venues promote student gambling: Bay Meadows racetrack advertises in college newspapers while local card clubs hire college students to work as prop players. Meanwhile, credit cards enable students without extra cash to gamble even after accumulating debt.

"People who are young are characteristically risky with drugs, alcohol, sex, and gambling," says Christine Reilly, a researcher at the Harvard School of Medicine's Division on Addiction, "and are at a higher risk of these behaviors developing into addictions."

A high-profile sports betting scandal at Northwestern University that drew national attention in 1998 prompted the National Association of School Personnel and Administrators (NASPA) to conduct a study on the prevalence and impact of college gambling. The results of the study, which surveyed students at seven universities, are still being compiled. But NASPA researcher Ken Winters, Ph.D., says young people are attracted to the thrill of betting.

"During the last five years we have seen a lot of study about adolescent gambling at the high school level," Winters says. "This makes public health people wonder, 'Well, if it's happening in high school then it must be happening in college.'"

And it is. Gambling is regarded as benign, as a rite of passage unrelated to addiction. Stories of students who take home big winnings only encourage other students to try their luck. Those who lose big have a great story to tell their friends, a story that begins with how much they were up when they should have cashed out. According to Ed Looney of the New Jersey Council on Compulsive Gambling, college students consider gambling more acceptable than drinking.

Santa Clara University senior Jeff Marinacci doesn't regard gambling as a problem. On a January trip to Reno he arrived at the tables with a few hundred dollars. But he and three cohorts won big -- so big, that Marinacci skipped his ride home for a couple more hours in the casinos. With $6,500 in winnings, they rented a black stretch limo to make the four-hour drive home.

"Every time I go up," Marinacci says, "I think I'm going to win."

But while Marinacci doesn't seem concerned about developing an addiction, experts on addiction are. A study conducted by Clayton Neighbors, PhD, professor of psychology at University of Washington, identified about 15 percent of college students as at least at risk for gambling problems. This number is much larger than the general population's, which Neighbors says runs between three and five percent.

Once these students develop a problem, half will become compulsive, according to Tom Tucker, director of the California Council on Problem Gambling.

"Students are doomed to be the next generation of problem gamblers without prevention education at the college level," Tucker says.

Researcher Durand Jacobs, PhD, a clinical professor of medicine at Loma Linda University, says lack of exciting entertainment contributes to the number of students who try gambling.

"Young males seek excitement from pervasive boredom," Jacobs says. "Gambling is like an upper drug, such as cocaine. It produces abnormal arousal levels."

In fact, a study published by a team of researchers in the journal Neuron found that gambling affects the brain in the same way as cocaine. According to the study, the areas of the brain stimulated by the anticipation and experience of gambling are similar to those stimulated by euphoria-inducing drugs.

This seems even more true for men. There are nine males with gambling disorders for every female, according to Dr. Kim Bullock of the Stanford University Medical Center. Bullock, who studies impulse control problems, says gambling disorders in men parallel compulsive shopping disorders in women.

"Men gain their self-esteem by what they can provide for their family monetarily," Bullock says, "so that may be why men go for gambling."

Bullock attributes the low recovery rates for gambling disorders partly to genes that predispose people to risk-taking and to depression. Gambling addicts may bet to fill an emotional void caused by underlying depression.

Filling that void becomes easier as opportunities to gamble increase – and they are increasing, especially with the planning of an Oakland Indian casino. The casino, on the site of the former Oakland Army Base, would undoubtedly attract local college students -- especially those at nearby UC Berkeley.

"I could see how students would get more involved with gambling, given the possibility of a closer casino," says Karen Kenney, Dean of Students at UC Berkeley.

Kenney is also concerned that chapters of Berkeley's large Greek system and athletic teams would host events at the new casino, something other Bay Area schools already do. Members of the Stanford's Sigma Chi fraternity make regular trips to the nearby Bay Meadows race track. The group takes advantage of a promotion called "Friday Alive," which boasts $2 big beers and $1 admission to go with the rush of betting on the horses.

"It's exciting to put money on it," says Brian Kreiner, the fraternity's social chair. "When people are excited about the outcome of the races it creates an exciting atmosphere."

Bay Meadows has been targeting students with advertisements in local campus newspapers for the past three years.

"They're dancing and having a couple of beers," says Bay Meadows Vice President Mike Ziegler. "It's not threatening."

Other local establishments, like Santa Clara's Garden City card club, also attract college students, but not with advertising. Instead, they offer them jobs. Network Management, a company associated with Garden City, pays several Santa Clara students $15 an hour to play Pai Gow poker as prop players. The students are trained to play poker with the club's money to get more money to change hands.

Opportunities to make money at local gambling sites entice students to experiment with gambling. Santa Clara University sociology professor John Ratliff, who researches online behavior, says increased opportunity inevitably increases the number of students who try gambling.

Ratliff also says access to technology provides students with more chances to start gambling. With over 1,400 Internet casinos just a click away, college students can use the high-speed Internet connections in campus dorms to place bets on anything from the Super Bowl to Yahtzee.
Currently, all online casinos are based in offshore locations like the Caribbean, Australia and the United Kingdom. In a matter of minutes, users can download software or log onto a server to access casino games. Operators make the sites as user-friendly as possible, accepting credit cards, debit cards, personal checks or wire transfers to establish a balance with offshore sites. The sites mimic the look and feel of Vegas: sounds of chips stacking and slots ringing, effervescent colors and simulated card tables.

Reilly says because young people are comfortable using the Internet, online gambling is a problem for their age group.

"The Internet is quick and easy and offers instant gratification," she says. "It leaves you very little time to think. You just act without noting the drawbacks. It offers anything you want."

Though the Justice Department says Internet gambling is still illegal in the United States, Nevada lawmakers recently voted to approve online gambling. The bill went to Gov. Kenny Guinn's desk after a 17-4 state Senate vote on June 4. Earlier this year, Congressman James Leach (R) of Iowa, , sponsored a bill called the Internet Gambling Funding Prohibition Act, which prohibits online casinos from accepting credit cards and other electronic forms of payment.

"Particularly vulnerable are young people," says Leach, former chairman of the House Banking Committee "who are members of the most literate computer generation."

Currently, the newly formed Financial Services Committee, which combines the old Banking committee with the securities and insurance jurisdiction of the old Commerce Committee, is holding hearings on the issue under the chairmanship of Rep. Mike Oxley.

Random number generators are supposed to provide fair odds while regulatory commissions serve as watchdogs for many of these offshore operations. But Julius Kiss, Director of Operations for Internet Gaming Software Solutions, questions the legitimacy of these sites.

"If I'm a casino operator, I can actually watch the game you're playing," says Kiss, whose Canadian company designs Internet gambling software. Kiss says operators can monitor games and alter what cards are dealt to players, making these offshore sites suspect.

But the possibility of foul play doesn't seem to deter students from gambling on the Internet. College-age gamblers will help online casinos earn an estimated $2.3 billion in revenue in 2001, according to the National Gaming Impact Study Commission Report.

Much of that revenue is earned by online sports books. The FBI estimates that over $3 billion was wagered on the 1999 NCAA Men's Division I Basketball championship, and each year, more of those bets are made online. But some college students, who get in on the action especially during the NCAA tournament and other big events, still rely on campus bookies to place bets.

"Scott," a Santa Clara senior started taking bets after reading a Hustler magazine article on bookmaking. He and a partner began making $8,000 a week but eventually quit because the business was getting so big, it became a full-time job.

"I would get calls constantly, all day long, people wanting to bet," Scott says. "And it doesn't matter where you are, you have to take the bets."

If caught, bookmakers must pay back the funds for the first offense and also a $500-$5,000 fine and serve up to one year in prison for the second offense, according to Section 337a of the California penal code.

WITH GRADUATION JUST a few days away, John Kollus spends his nights at the bar and his days at the pool, just like many of his Santa Clara classmates. However, unlike his peers, Kollus is shouldering a $10,000 debt, most of which he attributes to gambling.

The senior recalls a December trip to Tahoe with fraternity brother Jeff Kopaceck. Plans for a relaxing weekend changed as Kollus bolts for the casino the second they parked the car.

"I was like, 'I can't hold back,'" he says.

After a few hours at the tables, Kollus and Kopaceck were up $400. Redbull and vodka fueled increasingly aggressive betting. Yellow ten-dollar chips thrown on double-down hands were replaced by black hundred-dollar chips. They were beyond drunk -- they were drunk enough to believe they could beat the game.

"It's the alcohol, man," Kopaceck says. "If there were no drinking in casinos, people would lose nothing,"

Kollus recalls filling out credit card applications he received in the mail during his freshman year. Those two credit cards, which now carry a combined balance of around $10,000, have seen their share of casino ATMs. They've also enabled Kollus to gamble the way he likes: big.

Forty to sixty percent of cash wagered in casinos is withdrawn out of ATMs, either from personal accounts or as cash advances from credit cards, according to the National Gambling Impact Study Commission Report. Credit card companies are not required to report amounts borrowed for gambling.

On a spring break trip to Las Vegas, Kollus called his credit card company to request a $1,000 extension. After making him wait a few minutes for approval, they granted it to him, along with another $500 two hours later.

"It is easier to gamble for college students now, as credit cards are so easily accessible," Reilly says. "Companies are very aggressive towards college students with their marketing strategies."

Santa Clara resident Arul Chinnappan, a recent graduate of the University of Florida, never gambled until he received an email: "Congratulations Arul, you won $100!" Out of curiosity, he clicked on the gambling site and began playing blackjack. After an hour, $230 of his money was gone. The next day his email account showed 10 letters from on-line casinos offering money to play and six emails from credit card companies. After three months, Chinnappan owed credit card companies $12,000.

"Do college students have the money to be gambling with? No," Tucker says. "But if they have credit cards they do."

THERE WAS A time when "Brian" was afraid to answer the phone when it rang in his apartment two blocks from UC Davis. He knew it was his girlfriend, knew she was calling about their dinner plans in San Francisco. But he also knew he needed to save money to pay the credit card bills in front of him, which added up to about $8,000 – all from one bad month at the Reno Hilton Casino.

"Once you sit down in the chair and look at the cards, there is only one thing on the gambler's mind," Brian says. "And that is to win more."

But Brian didn't win, and quickly found himself thousands in the hole and unable to stop. It was only when his father confronted him about his habit that he was able gain control.

"He told me to either quit gambling or quit him," Brian says. "Knowing how hard my father worked in his life, I knew gambling was the last thing he would permit his son to do."

For most compulsive gamblers, it takes more than a lecture from Dad to put an end to such a serious problem. But the gap between numbers of college-aged pathological gamblers and those who seek treatment is sizeable. Approximately five percent of college students are compulsive gamblers, according to a meta-analysis study conducted at Harvard in 1997. But the Helpline Report for the California Council on Problem Gambling found that only 10 percent of all callers were between the ages of 21 and 25. Reilly says this indicates that college students often don't seek treatment.

"The numbers are still relevant, because we still continue to keep feeding estimates from other prevalent studies," Reilly says. "We continue to keep updating, and haven't seen any noticeable differences in the numbers."

Sandy, who asked her last name be withheld, became a compulsive gambler while working in card rooms for 10 years. Today, she is a public relations manager for Gambler's Anonymous, which experts consider the most effective treatment. She says she "went back and forth with my addiction until I was finally able to follow the program. Not everyone can do it.

"It's an unbelievable addiction. You lose your home and your family. You want to die."

Ed Looney of the New Jersey Council on Compulsive Gambling, cautions that compulsive gambling, like most addictions, is an impulse disorder that can be treated only when the addict is willing to make lifestyle adjustments.

"It's so developed that you need to change yourself," Looney says, "And if you don't, relapse is a reality. Most people who come to self-help groups will relapse."

Looney, also a recovering gambling addict, says facing reality is the hardest step for compulsive gamblers to take.

But most college-aged gamblers don't seem ready to take that step. Marinacci still believes he can win every time he bets while Stanford Sigma Chi's see their Bay Meadows trips as harmless fun. Brian only quit after a threat from his dad but still wouldn't say he's completely done gambling. And when Justin has enough time, he makes the 30-minute drive to Lucky Chances, a card room in Colma, Calif., instead of betting on the Internet. He slips into lightweight Polo khakis, dress shoes and a short-sleeved shirt -- he likes to keep his arms free. He travels light, carrying only his cell phone and Chapstick: the weight of coin or keys is distracting. Eight hours later he returns home, unable to fall asleep. He replays each move he made that night, wondering what the outcome would have been had he played his cards differently. And although he knows he is at risk for developing a gambling problem, at this point he feels he can control it.

"I worry about if I'll be able to stop this," he says. "My parents voice concerns all the time. My mom hates that I play, every time she gives me money, she asks, 'Is this for gambling?' But I'm in college and I have so few responsibilities. I have the next 45 years of my life to work everyday."

SIDEBAR No. 1

You may have a gambling problem if:

- You spend a large amount of time gambling.

- You begin to place larger, more frequent bets.

- You have growing debts.

- You begin to pin your hopes on the "big win," that will solve all of your other financial problems.

- You promise to cut back on gambling.

- You refuse to explain your absences from home, or lie about where you have been.

- You feel frequent emotional highs or lows.

- You boast about your winnings, and make light of your losses.

- You prefer gambling to a special family occasion.

- You seek new places to gamble close to home, and when you are on vacation.

If you are concerned that you or someone you know fits the above profile contact: 1-800-
GAMBLER.

SIDEBAR No. 2

Statistics Concerning Gambling

- 63% of Americans approve of legalized gambling.

- 29% of adults say that gambling should be reduced or banned altogether.

- 22% of Americans say that legalized gambling should be expanded.

- 49% of those who have gambled within the last twelve months admit to losing money.

- 75% of adults disapprove of online gambling.

- Between 1994 and 2000, the number of gambling trips by Americans has increased 20%.

- In 1998, of the nearly 15,000 individuals employed by Indian casinos only 10% were Native American.

- The FBI estimates that an excess of $2.5 billion is wagered on the NCAA Tournament each year.

- Suicide rates are 200 times higher than the national average for compulsive gamblers and 150 times higher for their spouses.

SIDEBAR No. 3

A first-person look at what it takes to gamble online

I'll be dead by Tuesday.

That what I thought when I was told to investigate how online gambling works. The only reason I don't spend every weekend at Nevada casinos is because they're in Nevada. Otherwise, I love it. The way the cards feel in my hand; the way the free drinks taste sliding down my throat; the way a 20 dollar bill looks shooting down the little slot in the blackjack table just before the dealer deals me my debt. But online casinos can't duplicate those feelings, right? I was supposed to find out.

Lose your money to the best, I always say. Based on InternetCasinoRankings.com's ranking criteria -- software quality, customer service, fairness policies -- Captain Cook's Casino is the best. I jumped right to the site and clicked on the "DOWNLOAD NOW" icon. I installed the software in just over a minute and was ready to go.

The Captain, like most online casinos, allows you to play for fun before playing for real money. Give him some basic info and you quickly get a feel for how to blow your savings. Although upgrades let you to play 24 different games, only five are available with the basic download. I went straight for the blackjack table.

Ten minutes into the demo version, I'm relieved. Down $40, I hate online gambling. It's rigged, I've decided, and there's no way I could get sucked in to The Captain's wicked games. Twenty minutes later, I'm not so sure. After increasing my standard bet to $200, I'm up 1,700 demo dollars. Feeling lucky, I click on the large "REGISTER AS REAL

USER" button, throw them my credit card number (which I know by heart, unfortunately) and immediately have a limit of $500 not-so-demo dollars.

I'm normally pretty skeptical when pretending to gamble in casinos named after famous explorers, so I was convinced the demo mode's odds were better than the real odds. I called to check, but The Captain's customer service team, which is docked somewhere in the UK (they can't say exactly where for security reasons) didn't have many answers. They said to email headquarters, but they never emailed me back. Thank God. Their answer was likely to be the same as most of the 1400 offshore casinos: they use a random number generator to create true odds, in demo and real play mode. I would have convinced myself to play for real dough, and undoubtedly would have lost it all. I didn't, sticking to demo mode and eventually closing my real account.

Logic - and my mom, probably - say I should have deleted the software immediately. I didn't, but I will soon, when I get around to it.

Just a couple more hands.

Opening Statement

Chairman Michael G. Oxley

Committee on Financial Services

Subcommittee on Oversight and Investigations
July 12, 2001

"The Financial Aspects of Internet Gaming: Good Gamble or Bad Bet?"

Thank you, Madam Chairwoman. I commend you for calling today's hearing on a topic of utmost concern, the financial aspects of Internet gambling. While it may seem a good gamble for those who engage in it, experience shows it's often a bad bet in the end.

Today's hearing is intended to get the lay of the land. We'll learn from an economist's perspective how Internet gambling has grown in recent years. We'll learn from the State law enforcement perspective what power the States have to stop illicit gambling on the Web and what means are being taken by criminals to evade those efforts. We'll hear from those in the trenches, the psychologists and counselors who on a daily basis see the devastation caused by an unregulated industry operating in an unforgiving medium.

We'll hear from the big players in this Big Game of Chance—the large casinos, the State lotteries and the racing industry. We'll hear from the software providers—the enablers, without whose expertise and acumen Internet gambling could not exist. We'll hear from perhaps the most vulnerable population—college athletics, whose contests become fair game for gambling on the Internet, whose athletes are potentially compromised by the allure of cash payouts for throwing games or shaving points, and whose students—your kids and my kids—are potential victims of a too-easy, snake-in-the-garden enticement of big winnings that often results in financial losses that will trail them and their families for years.

Finally, we'll hear from the credit card companies, whose products are in most cases the instruments by which Internet gambling takes place. I am pleased to see that my Full Committee colleague and former Chairman of the Banking and Financial Services Committee, Mr. Leach, is in attendance, and I look forward to his questions and comments on that particular issue.

The Internet to many conjures up images of the Wild West—the frontier; new, unconquered horizons; seemingly unlimited potential. To those holding such a view, gambling is just part of the tableau. But instead of Gus and Tex, sitting at a back table at the Dead Eye Saloon engaged in a high stakes game of seven card stud, we've got little Jimmy sitting at the family computer, maxing out Mom's credit card trying to beat the spread on the Ohio State-UCLA game, as posted by a "virtual casino" based in the Netherlands Antilles.

Tex and Gus' card game often ended in a little "disagreement," best settled at ten paces in the middle of Main Street. Little Jimmy's losing football bet may result in financial hardship for his family, possible criminal prosecution—and maybe a month without "Dawson's Creek" for little Jimmy.

If "Little Jimmy" is truly a child, allowed free ability to gamble by some fly-by-night casino in the Caribbean or elsewhere overseas, then we have much cause to be concerned. If he is instead "Big Jim," with his pocketful of sports lines, wallet full of MasterCards and VISA cards, and access to the "casinos of the world" through the Internet without having to step away from the comfort of his own living room, we have the potential for disaster. Families can be ruined, savings lost. In a very real sense, we've gone from *High Noon* to *Wastin' Away in Margaritaville.*

I look forward to the testimony this afternoon, and to a continuing dialog as we tread this thorny—but necessary—path toward a solution to a troubling and growing threat to our nation's financial markets—and its families.

Madam Chairwoman, again I commend you, and I look forward to the testimony as this Committee completes its first step toward reining in this wild bronco called Internet gambling.

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Statement by

Representative James A. Leach

before the Financial Services Committee, Subcommittee on Oversight and Investigations, hearing on Internet Gambling

July 12, 2001

Madam Chair, thank you for holding this hearing. Your leadership on this issue is deeply appreciated. The growing problem posed by Internet gambling is one we ignore at our peril.

While it is unlikely that Internet gambling can be done away with entirely, it seems that only action taken at the federal level will be able to curb its enormous growth. Gambling on the Internet is fast becoming one of the most critical issues confronting thousands of American families. Even though Internet gambling is a relatively new industry, it is growing at an exponential rate. Gambling on the Internet generated $1.6 billion in revenue worldwide in 2000 and is projected to grow to $5 billion by 2003. Around 4.5 million Americans have gambled online and over a million gamble daily.

The Unlawful Internet Gambling Prohibition Act, H.R. 556, represents the most sensible approach to enforcement in this area. Tracking the settlement mechanism of financial instruments, like credit cards, is the only realistic approach that had been offered for quashing illegal Internet gambling.

Internet gambling, like other technology-related industries, has created a unique situation for law enforcement, financial institutions, and families. The simplicity and anonymity of the Internet has made populations that do not typically gamble vulnerable not only to one-time financial misjudgement but, in all too many cases, to addictive repeat betting where the odds are always in someone else's favor. In addition, the potential for criminal abuse by hackers, foreign money launderers and other gambling operators is far larger on the Internet than in licenced casino settings. Problem gambling made easy through the Internet can lead to serious psychological and physical as well as financial harms.

The 1999 National Gambling Impact Study Commission warned among other things, against the following: the potential for abuse by gambling operators who can alter, move or remove sites within minutes; the ability of hackers or operators to tamper with gambling software; and, a sense of anonymity which enhances the ease of money laundering. These threats are exacerbated by the fact that a substantial number of Internet gambling sites are located in unregulated offshore jurisdictions.

We tend to think of problem gamblers as individuals, rather than as members of families and communities--families and communities that are also affected by gambling and gambling-related problems. But problem gamblers do not exist in a vacuum. They not only precipitate problems for themselves and their immediate families, but problems for society: the wasting of potential investment and savings capital; bankruptcies that push interest rates and bank and credit card fees up; and increases in social services costs. It is a myth to think that gambling only effects

gamblers. Gambling losses and the resulting debt spill over to the financial and social services system and to those who may never engage in gambling.

On an individual level, problem gambling can lead to a large set of impacts, including physical stress reactions, like hypertension and heart disease, or severe psychiatric disorders. When someone's losses accumulate, family structures break down and the incidence of divorce and, even more tragically, suicide increase.

Gambling problems ripple down to all aspects of a gamblers life, including children and spouses. Family members of gamblers have a much higher occurrence rate of drug and alcohol abuse, stress reactions, and psychiatric disorders. Physical and verbal abuse is found more often in problem gambling families and the children of problem gamblers are more likely to gamble themselves.

There is a significant overlap between problem and pathological gambling and addictive disorders of various kinds. Large numbers of individuals who enter treatment for gambling programs report episodes of alcohol and drug abuse or dependance.

Debt is the most obvious side effect of gambling. The average debt for pathological gamblers in the 1980s ranged widely from $53,000 in New Jersey to $92,000 in Maryland. The tendency to accumulate tremendous debt is only aided by the ease at which people can gamble online. Wagering is becoming increasingly simple, as players enter in credit card numbers that enable

cash to be deducted directly from credit or bank accounts with a few clicks of a mouse. While in most instances, non-Internet gambling requires a person to take some sort of action before placing a bet, such as traveling to a casino, and losses are readily seen through a diminishing stack of chips, Internet gambling can be entered into easily and losses can quickly become manifestly larger than a wagerer or his family may have in mind as risk acceptable before sitting down at a keyboard.

Particularly vulnerable are young people, who are members of the most computer literate generation. While casinos have age limits for admission, there is no effective way to check the age of those betting over the Internet. This is an uniquely large problem on college campuses where students with a higher comfort level for computer technology can easily obtain credit cards through the mail or in student unions.

The seriousness of this situation on college campuses has manifested itself in a growing problem with betting on results and spreads in intercollegiate sporting events. Students may find their loan obligations related to tuition and books exacerbated by debts caused by gambling.

I am pleased to see the first financial industry representative here with us today. I have been astonished at the indifference and even anxiety to date of the credit card and financial intermediary community. Though it is clear that independent financial institutions will not be able to stop illegal Internet gambling alone, they have a profound interest in recognizing the magnitude of the problem and its effects on the industry and the economy as a whole.

There correlation between gambling and bankruptcy is potentially troubling. A problem gambler is almost twice as likely to file for bankruptcy than a non-gambler. For instance, in Iowa, 25 percent of people in gambling assistance programs have filed for bankruptcy, creating a ripple effect on non-gambling consumers. As bankruptcy rates, driven by consumer debt, increase in the United States, the implications for commercial businesses and intermediary financial institutions become more pressing. Similar to credit cards, bank loans fees and interest rates will increase in order to compensate for the added risk.

Indeed, prudent banks such as Wachovia, who we will hear from later, have begun to take it upon themselves to stop processing Internet gambling transactions because of the inherent risk of default, bankruptcy and fraud.

The significance of this private sector development must not be underestimated. Though there are costs associated with taking action to stop illegal Internet gambling, those costs are likely be less than the losses faced by the financial services industry due to gambling-related bankruptcies and defaults.

Financial intermediaries are in a unique position to extinguish the ripple being created by Internet gambling before the problem becomes endemic.

Accordingly, in this social context and because of practical implementation concerns, I have introduced the Unlawful Internet Gambling Funding Prohibition Act, H.R. 556, which is

intended to begin addressing this phenomenon. A similar bill was reported out of this Committee last Congress, but unfortunately was not considered on the House floor.

The measure prohibits gambling businesses from accepting bettors' credit cards, electronic fund transfers, or checks, in connection with illegal Internet gambling. Gambling institutions found in violation of the Act are subject to criminal and civil penalties. By attacking the settlement mechanism, the Act addresses serious issues confronting the general public, as well as the financial services community, as a result of the rapid worldwide growth of unregulated gambling over the Internet.

The bulk of Internet gambling sites are located offshore creating a unique enforcement situation. The Act does not unrealistically extend U.S. legal jurisdiction over other countries to specifically outlaw Internet gambling in those countries, but it prohibits settling bets through traditional credit card and bank instruments, thus restricting the ability of foreign gambling enterprises to operate in the United States.

Currently, under the Wire Act the U.S. Department of Justice may prosecute gambling operators who accept bets from U.S. residents via interstate telephone wires. Use of bank instruments by such gambling operators would be illegal under H.R. 556, subjecting these operators to criminal and civil penalties. The bill also empowers the federal banking agencies to issue orders prohibiting financial institutions from extending credit or facilitating an electronic payment to overseas individuals who are in violation of the Act.

H.R. 556 also calls on U.S. international negotiators to seek the cooperation of foreign governments in the enforcement of the Act and in determining the effects of Internet gambling on money laundering, corruption, and other international financial crimes. Because of the straight forward preclusion of use of standard aspects of the settlement mechanism, the approach contained in H.R. 556 would be an easily replicable model for other countries. A U.S. precedent would have the likely effect of setting an example for other countries to act in similar rather than discordant ways.

Several controversies have arisen around legislation addressing Internet gambling. Comprehensive gambling approaches -- as contrasted with payment process restrictions as embodied in H.R. 556 -- are susceptible to becoming bogged down with definitional and scope problems which make them vulnerable to being opened up to amendments which may authorize new types of gambling that are currently illegal. H.R. 556 can be considered as a stand-alone approach or in conjunction with other broader anti-Internet gambling initiatives if consensus in Congress can be achieved to go forward with broader new restrictions.

Greater legal restrictions on Internet gambling are in order and I support the efforts of Representatives Goodlatte and LaFalce and Senator Kyl to tighten the law in this area, but whether such efforts reach fruition, H.R. 556 is intended to be workable enforcement mechanism under current law or future law to give Federal and State authorities the tools they need to combat the social, economic and criminal implications of illegal Internet gambling.
Again, Madam Chair, let me stress how appreciative I am for your leadership on this issue and for calling this timely hearing.

OPENING STATEMENT OF
LUIS V. GUTIERREZ
RANKING DEMOCRAT
SUBCOMMITTEE ON OVERSIGHT & INVESTIGATIONS
THE FINANCIAL ASPECTS OF INTERNET GAMING:
GOOD GAMBLE OR BAD BET
JULY 12, 2001

Good afternoon Chairwoman Kelly and thank you for holding this important hearing.
Today, we are joined by a great number of experts who will share with us their knowledge and expertise in the area of Internet gambling. I hope that with the information and expertise gathered here today, we will be able to better address the issues concerning the rise of the Internet gambling industry. Approximately one million Americans gamble online every day and about 4.5 million Americans about five percent of those with access to the Internet have gambled online at least once.

Given the substantial number of people directly and indirectly affected by the future of Internet gambling, it is our job to guarantee that there are solid laws, secure technology and high-quality products in place.
Although most states allow some form of gambling activities, many states seek to prohibit online gambling because of the various problems associated with it. These include greater potential for fraud, increase in gambling addictions, protection of state tax revenues and children's easy access to gambling sites. I am particularly concerned about the ease with which children can access cyber-casinos.
In addition, we need to invest in prevention and treatment programs that will help gambling addicts and their families from the devastating impacts of this problem.

I look forward to hearing all of the testimonies.

**TESTIMONY OF DIRECTOR JOHN PETER SUAREZ
BEFORE THE HOUSE SUBCOMMITTEE ON OVERSIGHT
AND INVESTIGATIONS OF THE HOUSE COMMITTEE
ON FINANCIAL SERVICES
THURSDAY, JULY 12, 2001, 2:00 P.M.**

THANK YOU, MADAME CHAIRWOMAN, AND MEMBERS OF THE SUBCOMMITTEE FOR AFFORDING ME THE OPPORTUNITY TODAY TO SPEAK TO YOU REGARDING INTERNET GAMBLING. BEFORE ADDRESSING DIRECTLY INTERNET GAMING, I WOULD LIKE TO GIVE YOU SOME PERSPECTIVE, FROM A LAW ENFORCEMENT OFFICER AND REGULATOR, OF THE GAMING INDUSTRY IN NEW JERSEY.

GAMING WAS LEGALIZED IN NEW JERSEY IN 1977. OUR FIRST CASINO OPENED SHORTLY THEREAFTER, AND TODAY WE HAVE 12 CASINOS OPERATING EXCLUSIVELY IN THE CITY OF ATLANTIC CITY. LAST YEAR, THOSE 12 CASINOS DIRECTLY EMPLOYED NEARLY 50,000 PEOPLE, AND GENERATED REVENUE OF $4.4 BILLION. BY SOME ESTIMATES, OVER 34 MILLION PEOPLE VISITED ATLANTIC CITY LAST YEAR, MAKING IT ONE OF THE MORE POPULAR DESTINATIONS IN THE UNITED STATES. IN TERMS OF GAMING REVENUE,

ATLANTIC CITY'S 12 CASINOS ARE SECOND WORLDWIDE ONLY TO LAS VEGAS.

THE INTERNET COULD CHANGE ALL OF THAT. BY OUR ESTIMATES, THERE ARE WELL OVER 1,000 INTERNET CASINOS, LOCATED PREDOMINANTLY IN OFF-SHORE LOCALES SUCH AS ANTIGUA AND THE NETHERLANDS ANTILLES. THE TYPICAL INTERNET CASINO, THOUGH "LICENSED" BY THE HOST COUNTRY, FACES NONE OF THE REGULATORY SCRUTINY THAT IS NORMALLY ASSOCIATED WITH A LAND-BASED ENTITY IN THE UNITED STATES. INDEED, I SUBMIT THAT MANY OF THE OPERATORS OF OFF-SHORE CASINOS SEEK OUT THE JURISDICTIONS WITH THE "LOWEST COMMON DENOMINATOR" OF REGULATORY SCRUTINY, MOVING THEIR OPERATIONS TO THE PLACES WHERE THEY ARE LEAST LIKELY TO BE THOROUGHLY SCRUTINIZED. THESE OFF-SHORE CASINOS PAY LICENSING FEES TO THE HOST COUNTRY, AND THEN OPERATE THEIR SITES FREE FROM MEANINGFUL GOVERNMENT OVERSIGHT.

THE RISKS OF UNREGULATED INTERNET GAMING, OR POORLY REGULATED GAMING, SHOULD BE WELL KNOWN TO EVERYONE HERE: NO

MEANINGFUL LIMITATIONS ON PARTICIPATION BY UNDER-AGED GAMBLERS OR PROBLEM GAMBLERS; NO ASSURANCE AS TO INTEGRITY OF THE OPERATORS OR THE GAME; MONEY LAUNDERING ISSUES; PROTECTION AGAINST SECURITY BREACHES, HACKING, AND INFORMATION THEFT, TO NAME THE MORE SALIENT CONCERNS. FROM AN ECONOMIC STANDPOINT, INTERNET GAMING AS IT EXISTS TODAY ALSO FAILS TO PROVIDE ANY POSITIVE BENEFIT TO THE UNITED STATES, EITHER IN THE FORM OF TAX INCOME OR JOBS.

IN ADDITION TO THESE CONCERNS, FROM NEW JERSEY'S PERSPECTIVE, THE FUNDAMENTAL PROBLEM WITH OFF-SHORE INTERNET CASINOS, IS THAT BY ACCEPTING WAGERS FROM NEW JERSEY RESIDENTS, THEY VIOLATE NEW JERSEY'S CONSTITUTION AND LAWS REGARDING GAMBLING.

THE NEW JERSEY CONSTITUTION EXPRESSLY PROVIDES THAT "NO GAMBLING OF ANY KIND SHALL BE AUTHORIZED . . . UNLESS THE SPECIFIC KIND, RESTRICTIONS, AND CONTROL THEREOF HAVE BEEN . . . AUTHORIZED BY A MAJORITY OF THE VOTES CAST BY THE PEOPLE . . . .". SEE *N.J. CONST.* ART. IV, § 7,

¶2. IN ORDER FOR CASINO GAMING TO BE APPROVED IN NEW JERSEY, A CONSTITUTIONAL REFERENDUM WAS REQUIRED TO BE PASSED. THE QUESTION OF INTERNET GAMING HAS NEVER BEEN PUT TO THE PEOPLE, AND IS SIMPLY NOT PERMITTED, AND THEREFORE REPRESENTS A VIOLATION OF OUR CONSTITUTION AND OUR CRIMINAL AND CIVIL LAWS.

SOME HAVE ARGUED THAT IN ORDER TO COMPLY WITH NEW JERSEY'S LAW, LEGISLATION COULD BE CRAFTED THAT WOULD ALLOW THE EXISTING CASINO LICENSEES IN NEW JERSEY TO OPERATE INTERNET GAMING SITES WITH THE HOST SERVER LOCATED IN ATLANTIC CITY, THEREBY ELIDING THE CONSTITUTIONAL REQUIREMENT OF A PUBLIC REFERENDUM. IN FACT, THERE IS CURRENTLY PROPOSED LEGISLATION IN NEW JERSEY THAT WOULD PROVIDE FOR JUST THIS SCENARIO.

IN OUR VIEW, IT IS A RATHER LARGE CONSTITUTIONAL LEAP TO ARGUE THAT INTERNET GAMBLING FALLS WITHIN THE EXISTING CONSTITUTIONAL PROVISION AUTHORIZING CASINOS WITHIN ATLANTIC CITY. ALTHOUGH THE

PROPOSED LEGISLATION REQUIRES THAT A LICENSED ATLANTIC CITY CASINO OPERATE THE INTERNET SITE, UNDER THE BILL, THE BETTOR OR THE TERMINAL FROM WHICH THE BETS ARE PLACED MAY BE LOCATED ANY PLACE IN THE STATE.

TO ALLOW NEW JERSEY RESIDENTS TO ENGAGE IN CASINO GAMING FROM ANY LOCATION WITHIN THE STATE, RATHER THAN EXCLUSIVELY IN ATLANTIC CITY, WOULD REPRESENT A FUNDAMENTAL SHIFT IN THE PUBLIC POLICY OF OUR STATE, AND WOULD COMPLETELY REDEFINE THE GAMING ENVIRONMENT. SUCH DRAMATIC SHIFTS IN PUBLIC POLICY CANNOT AND SHOULD NOT BE ACCOMPLISHED MERELY BECAUSE THE ACTIVITY TAKES PLACE ON THE INTERNET. INSTEAD, CONSTITUTIONAL REQUIREMENTS IN OUR STATE MUST BE ABIDED, AND THE VOTERS MUST DECIDE WHETHER OR NOT THEY WANT SUCH A VAST EXPANSION OF CASINO GAMING IN NEW JERSEY.

INDEED, WHEN YOU CONSIDER SOME OF THE STATED PUBLIC POLICY OBJECTIVES TO BE ACHIEVED IN ALLOWING CASINO GAMING IN ATLANTIC CITY,

YOU QUICKLY REALIZE THAT INTERNET GAMING SIMPLY CANNOT MEET THOSE GOALS, NO MATTER WHERE OR HOW IT TAKES PLACE.

WHEN GAMING WAS APPROVED BY REFERENDUM, ONE OF THE EXPRESS PURPOSES WAS TO ALLOW FOR THE REINVIGORATION OF THE TOURISM INDUSTRY IN ATLANTIC CITY AND TO REVITALIZE THAT CITY THROUGH THE BUILDING OF HOTEL ROOMS AND INFRASTRUCTURE DEVELOPMENT. A VIRTUAL CASINO CONTRIBUTES NO HOTEL ROOMS, ANCILLARY BENEFITS OR DEVELOPMENT TO THE CITY, AND CAN SATISFY NONE OF THE PUBLIC POLICY GOALS ENUNCIATED.

THUS FACED WITH AN INDUSTRY THAT IS IN VIOLATION OF NEW JERSEY'S LAWS AND CONSTITUTION, AND IS CONTRARY TO THE EXISTING PUBLIC POLICY OF THE STATE, NEW JERSEY HAS INSTITUTED LEGAL PROCEEDINGS TO STOP INTERNET GAMING COMPANIES FROM ACCEPTING OR SOLICITING WAGERS FROM NEW JERSEY RESIDENTS.

IN JUNE OF THIS YEAR, THE DIVISION OF GAMING ENFORCEMENT AND THE DIVISION OF CONSUMER AFFAIRS TOOK THE UNUSUAL STEP OF FILING CIVIL COMPLAINTS AGAINST THREE SUCH INTERNET CASINOS SEEKING TO ENJOIN THEIR ACTIVITY AND TO HAVE THE COURT IN NEW JERSEY ORDER THAT THE SITES PERMANENTLY EXCLUDE NEW JERSEY RESIDENTS. THESE THREE PARTICULAR INTERNET CASINOS WERE IDENTIFIED BECAUSE THEY HAD ADVERTISED ON BILLBOARDS THROUGHOUT THE STATE OF NEW JERSEY, AND ACTIVELY SOLICITED RESIDENTS OF NEW JERSEY TO WAGER WITH THEM. TWO OF THE SITES OFFERED BOTH CASINO STYLE GAMES AND SPORTSBOOK WAGERING, AND THE THIRD SITE OFFERED ONLY CASINO STYLE GAMES.

IN OUR ACTIONS, WE HAVE ALSO ASKED THAT THE COURT ORDER THE SITES TO PROVIDE AN ACCOUNTING TO US OF ALL WAGERS MADE BY NEW JERSEY RESIDENTS, AND WE HAVE ALSO SOUGHT THE RECOVERY OF ALL FUNDS LOST BY NEW JERSEY RESIDENTS.

AFTER WE WIN THESE THREE CASES, WE ONLY HAVE ABOUT 997 MORE TO

GO. AND THEREIN LIES THE PROBLEM FOR US. ALTHOUGH WE FULLY BELIEVE THAT OUR CASES CAN AND WILL BE WON, THEY WILL PRESENT INTERESTING ISSUES FOR THE COURTS, AND IN THE TIME THAT THE LITIGATION IS PENDING, THE OFF SHORE CASINOS WILL CONTINUE TO OPERATE AND PROLIFERATE.

ONE OF THOSE INTERESTING ISSUES, AND ONE THAT PROPONENTS OF INTERNET GAMING OFFER TO DEFEAT CLAIMS THAT THEY ARE IN VIOLATION OF EXISTING LAW, IS THE QUESTION OF JURISDICTION. AS MANY OF THE MEMBERS KNOW, OFF-SHORE CASINO OPERATORS CONTEND THAT THEIR SITES DO NOT VIOLATE FEDERAL OR STATE LAW BECAUSE THE WAGERS ARE "PROCESSED" IN A HOST COUNTRY WHERE SUCH WAGERING IS LEGAL. ACCORDINGLY, THEY ARGUE THAT THERE IS NOTHING LEFT TO BE DONE BY THE STATES OR FEDERAL GOVERNMENT.

THIS ARGUMENT IS, QUITE SIMPLY, NONSENSE.

IN NEW JERSEY, AS FAR BACK AS 1953, OUR STATE SUPREME COURT HELD

THAT WHERE INDIVIDUALS USE THE TELEPHONE TO TRANSMIT WAGERING INFORMATION, BOTH THE WAGERER AND THE RECIPIENT ARE ENGAGED IN ILLEGAL BETTING. THIS REMAINS THE LAW IN NEW JERSEY TODAY, AND INDEED IS A FAIRLY BASIC PREMISE UPON WHICH TO FIND JURISDICTION AGAINST INTERNET GAMING COMPANIES. THE FEW CASES OF WHICH I AM AWARE THAT HAVE DIRECTLY ADDRESSED THE ISSUE OF INTERNET GAMING AND JURISDICTION HAVE ALL FOUND THAT JURISDICTION CAN AND DOES LIE IN THE PLACE WHERE THE BETTOR IS LOCATED, AND NOT WHERE THE SERVER IS FOUND. IN FACT, THE DEPARTMENT OF JUSTICE HAS CONSISTENTLY HELD THAT VIOLATIONS OF THE FEDERAL WIRE ACT CAN OCCUR WHERE THE WAGER OR CALL IS MADE, AND IS NOT DEPENDENT ON WHERE THE ILLEGAL BET OR WAGER IS RECEIVED. SEE, E.G., *UNITED STATES v. COHEN, S.D.N.Y.; TESTIMONY OF KEVIN V. DIGREGORY BEFORE THE SUBCOMMITTEE ON CRIME ON THE JUDICIARY, DEPUTY ASSISTANT ATTORNEY GENERAL, JUNE 24, 1998.*

BUT EVEN WHEN WE DEFEAT THE CLAIMS ABOUT JURISDICTION, WE ARE LEFT WITH THE DIFFICULTY OF USING OUR EXISTING LAWS, WHICH WERE

NEVER MEANT TO ADDRESS DIRECTLY INTERNET GAMBLING. SO, FOR EXAMPLE, IN NEW JERSEY WE CAN PROCEED EITHER CIVILLY OR CRIMINALLY AGAINST OPERATORS OF INTERNET GAMING SITES, BUT CONFRONT DIFFICULTIES EVEN WITH THE SIMPLE TASK OF ATTEMPTING TO EFFECTUATE SERVICE OF PROCESS. IN OUR CURRENT CASES, WE ARE ATTEMPTING TO USE EVERY MEANS POSSIBLE, BUT THE PROCESS IS DIFFICULT AND TIME CONSUMING.

AND IN THE TIME THAT IT WILL TAKE US TO EFFECTUATE SERVICE, WE SUSPECT THAT MANY MORE NEW INTERNET GAMING SITES WILL OPEN FOR BUSINESS, LURING MORE OF OUR CITIZENS TO THEIR VIRTUAL CASINOS, AND TAKING FROM THEM REAL DOLLARS. CHANGES TO OUR EXISTING LAWS WOULD, IN MY VIEW, GREATLY ENHANCE LAW ENFORCEMENT'S ABILITY TO RESPOND TO THIS ISSUE.

BEFORE I SPEAK ABOUT POSSIBLE LEGISLATION, PLEASE LET ME ADD TWO CAVEATS. FIRST, ALTHOUGH UNDER CURRENT NEW JERSEY LAW,

INTERNET GAMING IS ILLEGAL, THIS COULD CHANGE WERE A CONSTITUTIONAL REFERENDUM TO BE PASSED. IN TESTIFYING HERE TODAY, I DO NOT INTEND TO BE ADVOCATING EITHER FOR OR AGAINST THE PASSAGE OF SUCH A REFERENDUM. AT THE FEDERAL LEVEL, ALTHOUGH SOME COURTS HAVE HELD THAT INTERNET GAMING VIOLATES THE WIRE ACT, A RECENT CASE IN LOUISIANA HAS THROWN THIS PROPOSITION INTO SOME DOUBT. NOTWITHSTANDING THAT HOLDING, AND REGARDLESS OF ALMOST ALL STATE LAWS RELATING TO GAMING, THERE IS LITTLE DEBATE BETWEEN REGULATORS, LAW ENFORCEMENT, AND THE REPUTABLE CASINO INDUSTRY REGARDING SPORTS BOOK WAGERING. EXCLUDING THREE STATES, SPORTS BOOK WAGERING IS SIMPLY ILLEGAL AS A MATTER OF FEDERAL LAW, AND HAS BEEN SO FOR NEARLY A DECADE. NO MATTER WHERE ONE STANDS ON THE SIDE OF INTERNET GAMING, THERE IS LITTLE DISPUTE THAT SPORTS BOOK WAGERING CANNOT BE PERMITTED VIA THE INTERNET ABSENT A CHANGE IN THE PROFESSIONAL AND AMATEUR SPORTS PROTECTION ACT AND THE FEDERAL WIRE ACT.

AS FOR LEGISLATION, THERE ARE TWO OBVIOUS CHOICES FACING STATES AND THE FEDERAL GOVERNMENT, AND THEY ARE EITHER PROHIBITION OR THE IMPOSITION OF A REGULATORY MODEL SIMILAR TO THAT USED FOR LAND-BASED CASINOS. SHOULD A DECISION TO ALLOW AND REGULATE INTERNET GAMING BE MADE AT THE STATE OR FEDERAL LEVEL, THEN THERE ARE MANY METHODS TO ENSURE THE CHARACTER OR FITNESS OF INTERNET OPERATORS AND TO PROTECT THE PUBLIC. ALTHOUGH NO REGULATORY MODEL COULD EFFECTIVELY PREVENT DISREPUTABLE OPERATORS FROM LURING PLAYERS, REGULATORS COULD INSURE THAT SITES OPERATING LEGALLY WITHIN A JURISDICTION SATISFY WHATEVER LICENSING STANDARDS THAT THE PARTICULAR JURISDICTION FEELS ARE NECESSARY TO ENSURE INTEGRITY OF THE GAMES.

IF PROHIBITION OF INTERNET GAMING IS CHOSEN AS THE COURSE OF ACTION BY AN INDIVIDUAL STATE OR BY THE FEDERAL GOVERNMENT, THEN THERE ARE ALSO SEVERAL WAYS IN WHICH SUCH A PROHIBITION COULD BE ENFORCED.

I KNOW THAT MOST PROPONENTS OF INTERNET GAMING HAVE DECLARED THAT A PROHIBITION SUCH AS THAT PROPOSED BY THE KYL BILL WOULD BE IMPOSSIBLE TO ENFORCE, AND HAVE CLAIMED THAT THE BILL'S DEFEAT IN CONGRESS' LAST SESSION WAS A VICTORY FOR REALITY OVER FUTILITY.

AS A FORMER FEDERAL PROSECUTOR AND THE DIRECTOR OF THE DIVISION OF GAMING ENFORCEMENT RESPONSIBLE FOR THE LAWS OVERSEEING THE CASINO INDUSTRY IN THE STATE OF NEW JERSEY, I UNDERSTAND THE NEED TO HAVE LAWS IN PLACE THAT CAN BE EFFECTIVELY ENFORCED, AND THAT A PROPOSAL THAT CANNOT BE ENFORCED DOES NOT SERVE THE INTERESTS OF LAW ENFORCEMENT OR THE BODY POLITIC.

BUT IT IS ASTOUNDING TO ME HOW SOME CAN TRUMPET THE WONDERS OF TECHNOLOGY, AND CAN PRAISE THE GROWTH OF THE INTERNET AS INEVITABLE AND IRREVERSIBLE, AND AT THE SAME TIME DECLARE THAT TECHNOLOGY IS SIMPLY INCAPABLE OF EFFECTIVELY STOPPING INTERNET GAMBLING.

HOW DO THEY REACH THAT CONCLUSION? IS TECHNOLOGY INCAPABLE OF IDENTIFYING PEDOPHILES WHO SELL SUCH IMAGES ON THE WEB? OR IS LAW ENFORCEMENT INCAPABLE OF STOPPING SOMEBODY FROM PURCHASING ILLEGAL DRUGS OVER THE INTERNET? AND DO WE GIVE UP ON THOSE FRONTS SIMPLY BECAUSE THOSE WHO WOULD STAND TO GAIN FROM A CHANGE IN THE LAW HAVE DECLARED THE TASK IMPOSSIBLE?

AGAIN, MORE NONSENSE. OF COURSE THERE ARE WAYS TO CONTROL AND ENFORCE A PROHIBITION OF CERTAIN TYPES OF ACTIVITY, INCLUDING INTERNET GAMBLING, ON THE INTERNET. AS SOME CREDIT CARD COMPANIES HAVE DONE, THEY CAN REFUSE TO PROCESS CERTAIN WAGERS FROM COMPANIES THAT ENGAGE IN INTERNET WAGERING. WE CAN TAKE ENFORCEMENT ACTIONS AGAINST ISP'S THAT KNOWINGLY ALLOW FOR ACCESS TO INTERNET GAMBLING SITES.

OR THE U.S. CONGRESS OR STATE LEGISLATURES CAN SIMPLY DECLARE

THAT ANY CREDIT CARD OR OTHER WAGER PLACED VIA THE INTERNET IS ILLEGAL AND THEREFORE UNCOLLECTIBLE IN THE UNITED STATES. AND IF CONGRESS SO SPOKE, THE PROFITABILITY OF INTERNET GAMBLING WOULD BE SEVERELY ERODED. INDEED, SUCH A PROPOSAL WAS ENDORSED BY THE NATIONAL GAMBLING IMPACT STUDY COMMISSION, BUT HAS YET TO FIND PURCHASE IN THIS CONGRESS.

AND YET SOME DECLARE THE TASK IMPOSSIBLE WITHOUT EVER HAVING TRIED. IF THAT MENTALITY PERVADED THE DEVELOPMENT OF THE INTERNET, WE WOULD STILL BE USING TYPEWRITERS AND SENDING MESSAGES THE OLD-FASHIONED WAY, VIA SNAIL MAIL.

A MISTAKEN BELIEF IN THE IMPOSSIBILITY OF ENFORCING A PROHIBITION IS NOT A LEGITIMATE BASIS FROM WHICH SIGNIFICANT POLICY DECISIONS SHOULD BE MADE.

PERHAPS ILLEGAL INTERNET GAMBLING IS INEVITABLE, AND WE WILL BE

PROVEN WRONG. BUT I BELIEVE THAT SUCH A CONCESSION IS FAR TOO PREMATURE, AND THAT TO MAKE THAT CONCESSION NOW WOULD CHANGE THE GAMBLING LANDSCAPE IN WAYS THAT NONE, NOT EVEN THE PROPONENTS OF INTERNET GAMBLING, CAN FULLY APPRECIATE.

INSTEAD, IT IS MY VIEW THAT THE TIME IS UPON US TO ENGAGE IN A FULL DEBATE ON THIS ISSUE, AND TO DECIDE HOW, OR MORE IMPORTANTLY, IF, WE AS A SOCIETY WANT TO PROCEED WITH INTERNET GAMBLING. ONCE THE ANSWER IS CLEAR, THEN CAN WE BETTER DETERMINE WHAT THE NEXT STEP SHOULD BE. BUT WE SHOULD ENGAGE IN SUCH DECISIONMAKING NOW, RATHER THAN ALLOW INTERNET GAMING TO BECOME A REALITY FOR ALL US SIMPLY BY DEFAULT. IT IS FAR TOO IMPORTANT AN ISSUE WHOSE FATE SHOULD NOT BE DECIDED BY INACTION.

I THANK YOU FOR THE OPPORTUNITY TO PRESENT MY REMARKS, AND I AM AVAILABLE FOR ANY QUESTIONS THAT MEMBERS OF THE COMMITTEE MAY HAVE.

State of New Jersey

Department of Law and Public Safety
Division of Gaming Enforcement
P.O. Box 047
Trenton, NJ 08625-0047

Donald T. DiFrancesco
Acting Governor

John J. Farmer, Jr.
Attorney General

John Peter Suarez
Director

August 6, 2001

Janice Zanardi
Committee on Banking and Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

RE: Response to Questions Regarding Internet Gambling

Dear Ms. Zanardi:

I am in receipt of a letter from Hugh Halpern dated July 24, 2001, requesting additional responses to questions posed by Rep. Luis Gutierrez relating to my testimony before the Subcommittee on Oversight and Investigations on Internet gambling. Please accept this letter as my response to the additional questions posed.

1. **Could you expand on some of the efforts made by the International Association of Gaming Regulators to deal with problems associated with Internet gambling across jurisdictional borders?**

The International Association of Gaming Regulators ("IAGR") has not specifically addressed the issue of jurisdictional concerns related to Internet gambling. In the past, during our annual conference we have discussed and debated the issue, but no action has been taken by IAGR. This is partly a reflection of the differing attitudes towards Internet gambling held by our members, and is also due to the fact that IAGR is not charged with establishing policy or guidelines for its members, but instead provides a forum in which to exchange ideas and information. There is currently pending before our members a draft of a proposed position paper on Internet gambling, which endeavors to suggest certain minimum standards that an Internet gaming company should adhere to, but this position paper has not been considered or adopted by our full membership, and is therefore not available for further dissemination.

2. **What specific changes in current law would you suggest to effectively control access to illegal Internet gambling and at the same time enhance law enforcement's ability to respond to this problem?**

As has been indicated previously, illegal Internet gambling presents formidable obstacles to effective law enforcement because the vast majority of providers of Internet gambling operate from outside the United States. Criminal penalties should nevertheless exist for such providers and, in this regard, if the government were to endorse a prohibition, the Wire Act would need to be amended to clarify that the transmission of information or data related to casino style games, in addition to sports wagering information, would violate federal law.

However, recognizing that the practical effectiveness of criminal legislation will be limited by the inability of United States law enforcement authorities to reach offshore Internet gambling operators and their assets, and that foreign governments that receive tax revenues from Internet gambling will likely be unwilling to assist in prosecutorial efforts, prohibitory legislation would have to focus on the United States-based components that make illegal Internet gambling both possible and profitable.

First among these are the financial services which essentially provide the money supply for illegal offshore Internet gambling operations. The federal government could provide that all credit card transactions used to facilitate Internet gambling are void and unenforceable, and that efforts to collect such debts and obligations shall be prohibited. The government could further declare that no financial instruments, such as checks, wires, credit cards, money transfers, or other instrumentality shall be used to facilitate in any capacity Internet gambling.

I believe that the elimination of the use of credit cards in Internet gambling transactions would likely have the greatest impact, as most casual or recreational gamblers will use a credit card to facilitate wagering at an online casino. Although some patrons and Internet gambling sites would avoid this problem by using a financial instrument such as a check or wire to deposit funds for account wagering, if a provision barring the use of credit cards and financial instruments were adopted, then it is likely that the overwhelming majority of sites soliciting wagers from United States residents would be rendered unprofitable.

A second component of an effective prohibitory policy would be the Internet service providers, makers of wireless communication systems, ancillary technical support services, software designers, or any other business or individual whose product or service facilitates illegal Internet gambling. A law enforcement strategy including such a component was expressly recommended in the Report of the National Gambling Impact Study Commission at 5-12 (June 18, 1999).

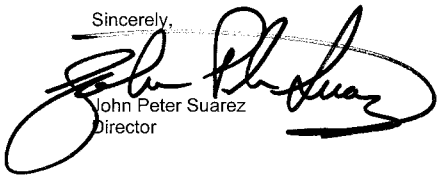
A final target of effective prohibitory legislation could be the media, including computer-based, broadcast and print, which facilitate the operation of illegal Internet gambling by running commercial advertisements for such gambling operations. Notwithstanding the constitutional protections for ordinary commercial advertising, a

prohibition on advertising products or services that are illegal may well prove to be constitutional and effective.

* * * * * * *

I hope that these answers are helpful to Rep. Gutierrez and the other members of the Subcommittee. Should you have any other questions or concerns, please feel free to contact me. Again, thank you for the opportunity to provide this testimony.

Sincerely,



John Peter Suarez
Director

c: John J. Farmer, Jr., Attorney General

State of New Jersey

Department of Law and Public Safety
Division of Gaming Enforcement
P.O. Box 047
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Donald T. DiFrancesco
Acting Governor

John J. Farmer, Jr.
Attorney General

John Peter Suarez
Director

August 22, 2001

Janice Zanardi
Committee on Banking and Financial Services
2129 Rayburn House Office Building
Washington, D.C. 20515

RE: Response to Questions Regarding Internet Gambling

Dear Ms. Zanardi:

The New Jersey Division of Gaming Enforcement is in receipt of a letter from Hugh Halpern dated August 7, 2001, requesting additional responses to questions posed by Rep. Sue Kelly relating to my testimony before the Subcommittee on Oversight and Investigations on Internet gambling. Please accept this letter as our response to the additional questions posed.

1. **Many believe that current law, including the Wire Act, makes Internet gambling illegal already. Do you agree with this interpretation of Federal law?**

In our view, there is no doubt that 18 U.S.C. § 1084 applies to Internet gambling as it relates to sports book wagering. As the Second Circuit Court of Appeals recently noted in upholding the conviction of Jay Cohen for operating an offshore Internet sports book, "[w]e need not guess whether the provisions of § 1084 apply to Cohen's conduct because it is clear that they do. . . ." U.S. v. Cohen, _ F.3d_, 2001 WL 863590, *8 (2d Cir. 2001). Indeed, the statutory language itself leaves little room for debate, and those entities operating Internet sports book sites that accept wagers from residents of the United States violate existing federal law.

There is some ambiguity as to whether or not casino-style games offered via the Internet also violate Federal law. Although the Department of Justice has consistently maintained that the Wire Act does cover this type of activity, the language of the Act does not lend itself to such an easy interpretation, and a Federal District Court has directly held to the contrary, In re Mastercard Int'l Inc., 132 F. Supp. 2d 468, 479-481 (E.D. La. 2001). Should a statutory change be proposed to the Wire Act, that proposal should clarify whether or not the Wire Act applies to casino-style wagering over the Internet.

Although you have asked me about our interpretation of Federal law, I must note that under existing law in New Jersey, both sports book wagering and casino-style games offered via the Internet violate New Jersey's Constitution and State law relating to gaming. Accordingly, casino and sports book wagering cannot be offered to New Jersey's citizens absent a legislative change initiated by a Constitutional amendment.

2. Some in the credit card industry claim they have no way to identify and stop transactions between Americans and illegal offshore Internet Gambling operations. Do you accept that argument? Can one argue that the credit card industry is "aiding and abetting" an illegal activity? Have you ever discussed with the credit card industry its role in illegal offshore Internet gambling?

The suggestion that credit card companies have no way to identify and stop transactions between Americans and illegal Internet gambling operations is at best misleading, if not downright false. It has been widely reported that a number of credit card companies have refused to process Internet gaming transactions and that those companies have effectively identified Internet gaming sites and prevented their cards from being used by offshore Internet gaming companies. For example, both American Express and Discover Card have longstanding policies of refusing to do business with any site that they know to be involved with online gaming.

In addition, both Visa and MasterCard have issued policy directives to their merchants that prohibit the payment of winnings from online gambling via their credit card, and also require online gambling sites to advise customers that they must ascertain the legality of Internet gaming in their respective jurisdictions. In addition, a number of banks issuing Visa and MasterCard, such as Bank of America, Providian, MBNA, Capital One and Wells Fargo, have informed merchants that they will no longer process transactions from Internet casinos.

As for aiding and abetting, if a person acts with the purpose of promoting or facilitating the commission of an offense, and aids or agrees to aid another person in committing the offense, then that person could be held liable for the offense under an aiding and abetting theory. In order to prove that a credit card company aided and abetted the illegal gambling activity, one would have to prove that the credit card company knew (or willfully blinded itself to the knowledge) that the charges presented for payment were used to conduct illegal gambling activity, and then facilitated the illegal gambling by processing the gaming transactions. To avoid liability, credit card companies could refuse to process transactions they know or should know are related to illegal Internet gaming, or they could seek to avoid liability by taking reasonable efforts to ensure that their cards were not used for criminal purposes.

3. In contrast to your recommendation that Internet gambling should be banned, Mr. Sinclair has argued that a ban will not work, just as Prohibition did not work in control of alcohol. He argues, instead, in favor of regulation of Internet gambling. Would you like to respond?

As is reflected in my written testimony, we do not advocate for or against a prohibition on Internet gambling. However, we do believe that a deliberate decision should be reached as to whether or not we as a society should allow Internet gambling, so that a coherent law enforcement strategy can be adopted. As indicated at the hearing, we believe that legislative leaders should consider all options, and should not choose regulation based upon the inaccurate assumption that it would be impossible to enforce a prohibition.

As far as the argument offered by Mr. Sinclair and others suggesting the futility of a ban on Internet gaming, we believe that such conclusions are at best premature, and are offered by those interested in seeing Internet gaming legalized in this country. Legislators could provide law enforcement with effective tools aimed at curbing Internet gaming, such as adopting the proposal from the National Gambling Impact Study Commission which suggests the passage of laws making "any credit card debts incurred while gambling on the Internet . . . unrecoverable. . . ." *See* Natl. Gambling Impact Study Comm. at 5-12. More expansive legislation could forbid the use of any financial instruments to satisfy Internet gambling debts, and could forbid collection efforts for debts incurred as a result of Internet gambling. Finally, legislation could also be crafted to target Internet Service Providers, and impose upon such providers the obligation to screen for sites offering illegal Internet gaming.

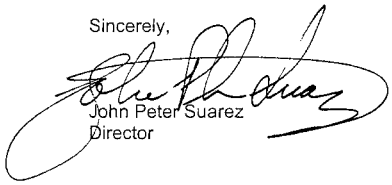
Legislation along the lines described above would provide law enforcement with significant tools to combat illegal Internet gambling. Although some will argue that even the legislative initiatives suggested here could be defeated by the most determined individuals seeking to gamble on the Internet, the profitability for gaming companies seeking to accept wagers from United States residents would be substantially impaired. Moreover, we fully believe that most United States residents are law-abiding citizens, and will, therefore, elect to forego illegal wagering, particularly where so many forms of legal gaming are already available. In short, the number of players willing to engage in steps to defeat a prohibition will necessarily be limited.

Of course, if a public policy decision is made to allow for regulated Internet gaming, then we believe that a regulatory model similar to those used now for land-based casinos should be adopted, and that operators of Internet gaming sites should be subjected to the same level of scrutiny as their land-based counterparts, to ensure that the public is protected and that the integrity of gaming operations is not compromised. We also believe that if a regulatory model is proposed, it must recognize that some jurisdictions will continue to make Internet gambling illegal, and must therefore require that operators take every effort to prevent access to their sites from jurisdictions where Internet gambling is not permitted.

* * * * * * *

We hope that these answers are helpful to Rep. Kelly and the other members of the Subcommittee. Should you have any other questions or concerns, please feel free to contact me. Again, thank you for the opportunity to provide this testimony.

Sincerely,



John Peter Suarez
Director

c: John J. Farmer, Jr., Attorney General

Statement of: Sebastian Sinclair
Vice President
Christiansen Capital Advisors, LLC
Before the Subcommittee on Oversight and Investigations of the House Committee on Financial Services
Washington, D.C.
Tuesday, July 10, 2001

Introduction

The Internet is the fastest growing telecommunications medium in history. In eight years, it has grown from virtually nothing to boast an estimated 151 million adult home users worldwide. It took only five years for the Internet to reach 50 million users. This compares to 38 years for radio, 13 years for television, and 10 years for cable. All forecasts for the future of this amazing medium predict continued growth.

On the other hand, the Internet has created some of the most vexing social problems ever encountered. The current social order, based on the premise of governments that rule over defined landmasses, has become complicated. In short, governing used to be directly related to real estate. Previously, physical location was used to determine legal (or illegal) activity. Someone from Utah, a State that has no legalized gambling, could gamble in a Nevada casino without fear of recrimination, and someone from Nevada could smoke marijuana in Amsterdam and the same rules applied. However, those lines on a map, once so important for governance, are blurred by the digital age.

The Internet has no geography. Distance is measured in nanoseconds and mouse-clicks, not miles and driving time. This lack of geography makes governance of the Internet difficult, particularly for goods and services that can be digitally delivered (such as pornography, music, movies, and gambling). Undaunted, however, some governments are attempting to dominate a global Internet with their own doctrines, dogma and practices (and the laws that develop from them). This would be fine if these governments and the nations they represent agreed on basic doctrines, dogma and practices. However, China does not like free speech, the United States does not like gambling, and most European nations like the Value Added Tax (VAT). To further complicate matters, governments are struggling with how to govern certain aspects of the medium (such as pornography, gambling, and taxation) without harming other activities that they view as beneficial.

Cyberspace itself is dangerously neutral; it has no predisposition toward what may be right or wrong. Built from the ground up to lack centralization, it may be built too well from the perspective of those that hold political power. It allows anyone to become a publisher of information or content that is easy to replicate and that reaches a global audience. This, in turn, makes the tracking and enforcement of copyrights difficult for their owners. It allows customers to quickly survey the offerings of thousands of suppliers, and purchase those goods tax-free. It eases communication, including terrorist communication. It allows for the global dissemination of products, offensive to some, such as pornography and gambling.

The balance between perfect freedom and perfect order has always been a delicate one; it is impossible to add or subtract from one side of that scale without proportionately influencing

the other. The creation of a global hard-to-regulate medium that will someday soon be available to nearly everyone has tipped that scale, maybe irrevocably.

It is in this environment that gambling over the Internet, or e-gambling, thrives.

The State of the Industry

More than a Medium

The foundation of globalization being built by the Internet has no architect; it is not so much by design but rather by accident that the world has become a much smaller place. And therein the problem lies; for all its promise and capacity for good this process underway is not without evils, the unique and chaotic formation and formulation of cyberspace has led to this final and inextricable globalization. Yet it's very nature, that which has fostered its astounding growth over the past decade, has become challenging for the protection of citizens and the enforcement of laws.

It would work well if our society had progressed as far as our technology, but the bottom line is that as we begin the 21st century society has a lot of catching up to do. The Internet is the true embodiment of egalitarianism. In cyberspace the weak are inseparable from the strong, the beautiful from the ugly. It is in this computer ether-world that cultures that have not yet learned to understand each other, let alone tolerate or get along, find themselves. Hindus mingle with Muslims, Muslims with Christians and Communists with Fascists. It is here that the 21st Century Barbarians at the gate of globalization accrue, not at IMF meetings, but on the Internet. The nucleus of all the "problems" associated with the Internet can be boiled down to one simple concept; regardless of whether we speak of pornography, taxation, human rights, or gambling, global society (if there is such a thing) differs on how to treat these issues. The individuals and institutions from different cultures are not ready to be in the same global boat despite the fact that that is where we find ourselves. It is unfortunate, but true that some of the individuals and institutions sailing toward this high tech frontier will try to push others, who possess different value systems, overboard.

This is dangerous ground that we tread. Increasingly, citizens and rulers in the 200 or so other countries of the world hear the word "Americanization" in place of "globalization" when the President and/or Bill Gates talk about the future. There appears to be widespread sentiment that globalization is a good thing, but as the United States moves forward in developing new efficient lines of lines of communications and commerce across multiple borders. Leaders would be wise to respect that laws and sensitivities of other cultures.

We know turn to the subject of e-gambling, global gambling, and the interactive future. While certainly not at the center of the social and cultural differences that have become so divisive in cyberspace, it is certainly not on the fringes either.

First off, e-gambling is anything but simple. It is an incredibly complex phenomenon that pits thousands of years of isolated cultural and societal evolutions and the social institutions that enforce these varying cultural standards with a technology that makes the enforcement of these standards difficult. Furthermore, it magnifies these cultural differences and calls question upon the legitimacy of institutions that can see the very same issues so differently.

Add to this mix a desire to gamble that seems hard wired in the human species and you have the nasty, foul-smelling brew that has spawned prohibitions, moratoriums, imperceptive political debate, and some hugely profitable businesses.

The American Experience with Gambling

As the United States National Gambling Impact Study Commission (NGISC) recognized, gambling, for the most part prohibited in the United States only a generation ago, is now a force in the economy and a pervasive presence in American life. Fifteen years ago, families choosing a vacation destination made Orlando the automatic choice; in 2001, Las Vegas is a viable option. Ten years ago, only a handful of computer users knew what the Internet was; and none of them gambled on it; now over 1,400 Web sites offer commercial gambling activities.

Consumers spent $61.4 billion on legal gambling in the United States in 2000 (Exhibit 1).[1] That is more than they spent on movie tickets, recorded music, theme parks, spectator sports, and video games combined. U.S. Gambling, Inc. (USGI), our fictional holding company for the nation's lotteries, casinos and other gambling businesses faired poorly in this expanding economy, however, dropping from 10th place in the 1999 *Forbes* Sales 500 to 12th in 2000, ahead of J.P. Morgan ($60.1 billion) and below Philip Morris ($63.28 billion). [2]

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[1] Christiansen, Eugene and Sinclair, Sebastian. The Gross Annual Wager of the United States-2000. http://www.cca-i.com/ Forthcoming.

[2] *Forbes*, "The Forbes 500s Annual Directory", April 16, 2001. http://www.forbes.com/.

Exhibit 1: 2000 U.S. Gross Gambling Revenues by Industry and Change From 1999

	1999 Gross Revenues (Expenditures) (revised)	2000 Gross Revenues (Expenditures)	Increase/(Decrease) in Gross Revenues (Expenditures)	
			Dollars	Percent
Pari-Mutuels				
Horse Totals	$3,382.9	$3,338.9	-$44.0	-1.30%
Greyhound Total	$489.7	$457.1	-$32.6	-6.65%
Jai Alai Total	$44.7	$46.6	$1.9	4.16%
Total Pari-Mutuels	$3,917.3	$3,842.5	-$74.7	-1.91%
Lotteries				
Video Lotteries	$1,397.0	$1,657.0	$259.9	18.61%
Traditional Games	$14,952.8	$15,558.7	$605.9	4.05%
Total Lotteries	$16,349.8	$17,215.6	$865.8	5.30%
Casinos				
Nevada/NJ Slot Machines	$8,739.8	$9,146.9	$407.1	4.66%
Nevada/NJ Table Games	$4,243.7	$4,407.6	$163.9	3.86%
Deepwater Cruise Ships	$273.4	$280.2	$6.8	2.50%
Cruises-to-nowhere	$318.8	$339.5	$20.7	6.50%
Riverboats	$8,340.0	$9,014.6	$674.7	8.09%
Other Land-Based Casinos	$787.3	$1,428.0	$640.7	81.37%
Other Commercial Gambling	$183.4	$171.0	-$12.3	-6.73%
Non-Casino Devices	$2,002.0	$1,558.2	-$443.9	-22.17%
Total Casinos	$24,888.4	$26,346.0	$1,457.6	5.86%
Legal Bookmaking				
Sports Books	$109.2	$123.8	$14.6	13.37%
Horse Books	$9.4	$6.8	-$2.6	-27.66%
Total Bookmaking	$118.6	$130.6	$12.0	10.12%
Card Rooms	$909.3	$949.3	$40.0	4.40%
Charitable Bingo	$1,044.6	$994.2	-$50.5	-4.83%
Charitable Games	$1,417.7	$1,483.8	$66.1	4.66%
Indian Reservations				
Class II	$1,149.8	$1,198.1	$48.3	4.20%
Class III	$8,464.9	$9,238.5	$773.6	9.14%
Total Indian Reservations	$9,614.7	$10,436.6	$821.9	8.55%
Internet Gambling	$1,167.0	$ 2,207.5	$1,040.5	89.16%
Grand Total	**$58,260.5**	**$61,398.6**	**$3,138.2**	**5.39%**

Notes: Columns may not add to totals due to rounding.
Because Internet gambling is conducted globally, gross gambling revenue from Internet gambling is not included in the grand total.

Christiansen Capital Advisors, LLC

Gambling businesses paid about $20 billion in taxes for the privilege of operating their commercial games in 2000.[3] Lotteries accounted for most of gambling's direct tax contribution, although gaming privilege taxes paid by casinos are significant to Nevada, New Jersey and the six riverboat casino states. In addition, as much as $3 billion went to Native American tribal governments fortunate enough to have a Class III (casino) facility.

The fact that Congress saw fit to impanel a National Gambling Impact Study Commission is an indication that quite a few people think this consumer choice may not be a healthy one. Many people feel Americans allocate too much of their incomes to gambling. On one side of the ledger are the quantifiable positive consequences of this consumer choice: the more than $20 billion in gambling privilege taxes the industries paid in 2000; the 400,000 or more jobs provided by the casino and pari-mutuel horse racing and breeding industries; the thousands of additional jobs provided by other pari-mutuel sports and lotteries as well as bingo halls and charitable operations; the capital invested in gambling businesses and the employment created by this investment on Wall Street. Also on the ledger's positive side is the difficult-to-quantify recreation that consumers derive from gambling: the fun ordinary people have playing bingo or blackjack or betting on the ponies.

But gambling's general ledger has a negative side. Some Americans believe gambling is sinful. Heavy consumer spending on commercial games is inconsistent with these beliefs and a source of discomfort for Americans holding them. Other Americans are persuaded that the costs of the operation of commercial games exceed the benefits. Some arguments commonly adduced to support this thesis are specious: for example, the oft-repeated assertion that "gambling is a sterile transfer of money that creates no new wealth."

The widespread acceptance of this argument makes a careful examination worthwhile. Demand, whether for shoes, PCs, Internet access, movies or blackjack, calls supply into being unless the state forbids suppliers to enter the market. The idea that commercial gambling is an exception to this economic law confuses one of the *macro-economic functions of commercial games*, the maintenance of a circulation of wagered dollars from one player to another, with the *economic consequences of supplying consumer demand for these games*. Bingo or blackjack or lotto games do indeed transfer money from one player to another, and, if they are friendly (i.e., non-commercial) games, that is *all* they do. In this sense, friendly games *are* "sterile": they produce nothing except recreation for the people who play them.[4]

But commercial games are not "sterile" in this sense, because they add a second macro-economic function to the activity of gambling: they extract a percentage of the circulating flow of wagered dollars and transfer it to the operator(s) of the game(s). The aggregate amounts thus transferred constitute the gross gaming revenues of gambling. These consumer expenditures on gambling call supply into being: they pay the wages and salaries of the hundreds of thousands of employees of the gambling industries, provide a

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[3] This figure represents gambling privilege taxes only, most gambling business also pay corporate income, property, and sales taxes as well, that are not included in this number.

[4] This claim is literally true for a friendly game of coin-toss, since the only equipment needed, a coin, is supplied by the mint. Friendly poker games oblige participants to buy cards and poker chips, as well as, perhaps, potato chips and beer; these direct and indirect friendly-game related consumer expenditures are inputs to the general economy but they are typically not funded by a percentage of the pot, an arrangement that would begin to move our poker game into the commercial category.

return on the equity component of the tens of billions of dollars invested in casinos and racetracks and companies that vend computerized wagering systems, service the debt component of these investments, support the stock prices of the hundred or so publicly owned companies involved with gambling, and, in sum, are the motivating force of an economic engine that is most visible in Nevada but that less visibly drives an annually growing portion of the United States leisure economy.

There are other arguments against allowing commercial games to operate that are not specious. The most important of these arguments is a "negative externality" that is peculiar to gambling: problem and pathological gambling behavior. There are hard costs, direct as well as indirect, to individuals and to society as a whole, of gambling that isn't fun and isn't play but a disorder. This disorder, which afflicts between 1% and 6% of North American populations exposed to commercial games, results in unaffordable losses and a long list of individual and social dysfunctions.

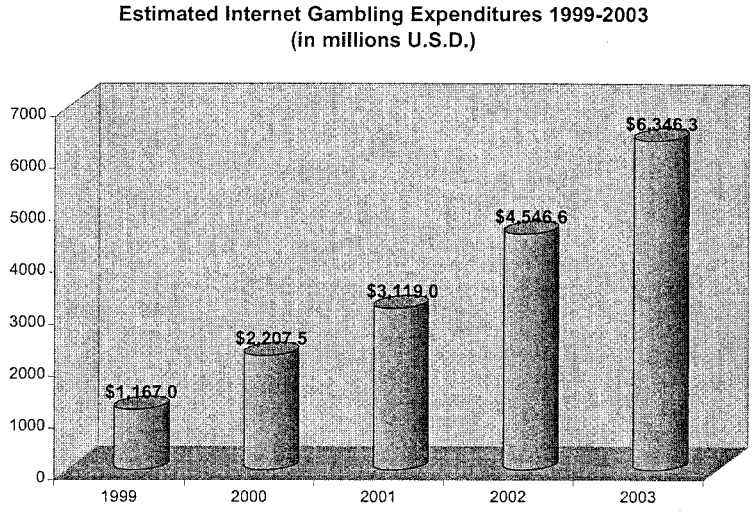
For lawmakers and for the development of rational public policy toward commercial games, it is important to understand how much problem gambling costs. The U.S. National Gambling Impact Study Commission determined that problem and pathological gamblers account for 15% of the industry's gross gambling revenues. Applied to the industry's $61.4 billion 2000 gross gambling revenues, this would amount to $9.2 billion.

These numbers go some way towards balancing the costs and benefits of gambling in the United States. Consumer spending on commercial games generated a $61.4 billion input to the U.S. economy in 2000 and that is a good thing. About 34¢ of every dollar of this consumer expenditure, or more than $20 billion, went to government in the form of gambling privilege tax. Many governments think that is a very good thing indeed, as do, we suspect, many taxpayers.

Gambling is prevalent in the United States. Only two jurisdictions Utah and Hawaii have no forms of legalized gambling. The numbers presented above convey the American appetite for commercial gambling games.

Until very recently that demand was serviced through ubiquitous lotteries, bingo halls or with pilgrimages to the nearest casino. Today gambling is available via the nearest Internet-enabled device. This has led to hyper-growth in the industry. Internet gambling increased by 89% in 2000; yet another record. The Internet has created the first global gambling market. Consumers, many of them Americans, spent an estimated $2.2 billion on e-gambling in 2000. We project this expenditure to rise to $6.4 billion by 2003 (Exhibit 2).

Exhibit 2: Estimated Internet Gross Gambling Revenues



Emerging Trends-Domestic and International

The Internet is reconfiguring all industries, not just gambling. At the leading edge, business models for securities trading, airline reservations, travel agencies, recorded music and a growing number of retail categories are being transformed, as Websites wring previously unsuspected inefficiencies out of pre-Internet methods of supplying these demands. At the trailing edge are goods that cannot be distributed or consumed in digitized form: agricultural products, transportation, energy, and smokestack industries like steel or manufacturing. Even in these sectors, however, the Internet is bringing new efficiencies to production and distribution.

Adjusting to the Internet has been a ragged process. Established businesses are seeing their markets altered overnight. Taxation and concepts of sovereignty are being tested and revised by the *force majeure* of Internet economics. Capital has poured indiscriminately into untried, often unsound business models. The so-called "New Economy" business failure rates are high and rising and yet the Internet wave continues to wash through the general economy undeterred.

At the heart of this process is *globalization*. Cyberspace is borderless, and Internet markets are inherently global. For governments this is an entirely new problem, one with few precedents for solution. "Walling off" a citizenry, as the Republic of China and Singapore

are trying to do, may prove impractical.[5] Collecting sales taxes on e-commerce goods and services is already problematic: a global tax structure for the global Internet marketplace is a possible solution, but one that implies global sovereign power to levy such taxes and global powers of collection and enforcement that do not currently exist. International treaties that were negotiated before digital property rights existed have been rendered obsolete, and rights in intellectual property--the basis for the communications and entertainment industries— are jeopardized by cyberspace. The scale of adjustment implied by the consequences of global Internet commerce is without precedent: not since the rise of nation-states have the fundamental assumptions underlying national sovereignty undergone such radical change.

Somewhere between the leading and trailing edges of the Internet wave lies gambling. Globalization has shifted the terms of the policy debate about gambling from social to economic imperatives and has led to the emergence of a highly competitive multinational industry.[6] Some likely impacts of globalization on legal gambling include the continuing fusion of gambling with popular culture and entertainment, major reorganization of the gambling industries, and further blurring of the boundaries between traditionally separate gambling enterprises.[7] Unsure of its legality and concerned for their licenses, established U.S. gambling suppliers have yet to embrace it. Elsewhere things are different. U.K. bookmakers and Australian gambling concerns, both public and private, have bowed to market forces and ported their businesses to the Web.

This is important; things have changed immensely since Senator Kyl first introduced legislation to prohibit Internet gambling. At that time, most of the jurisdictions authorizing and licensing the conduct of e-gambling were in the Caribbean, nations most famous for warm climates and their off-shore banking industry. Table 3 presents the nations that have authorized or allow some form of Internet gambling. Now 55 nations strong, that table is no longer dominated by St.-this or St.-that, but by recognizable 1st world nations: the United Kingdom, France, Australia, and Germany.

The emerging trend, domestically and internationally, is that the United States and the rest of the world may be walking down diverging roads.

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[5]Because these two nations have only one Internet Service Provider (ISP), the state, the prospects for the effective filtering of content are better than in a relatively fragmented and highly developed access market such as in the United States.

6 McMillen, J. 1996. "The Globalization of Gambling: Implications for Australia." The National Association for Gambling Studies Journal 8 (1): 9-19.

7 Austrin, T. 1998. "Retailing Leisure: Local and Global Developments in Gambling." In Time Out? Leisure, Recreation and Tourism in New Zealand and Australia, Perkins, C. C. & G. Cushman (eds.). Auckland: Longman. Pp. 167-181.

Exhibit 3: Legal Jurisdictions for E-gambling

Online Gambling Jurisdictions

Africa (4)
Anjouan , Liberia, Mauritius, Swaziland

Australasia (14)
Australian Capital Territory
Cook Islands
New South Wales, Australia
New Zealand
Norfolk Island, Australia
Northern Territory, Australia
The Philippines
Queensland, Australia
Solomon Islands
Tasmania, Australia
Vanuatu
Victoria, Australia
Vietnam
Western Australia

Caribbean (10)
Antigua and Barbuda
Curacao
Dominica
Dominican Republic
Grenada
Jamaica
Saba
St. Kitts and Nevis
St. Vincent
Trinidad

Central America (2)
Belize
Costa Rica

Europe (19)
Åland
Alderney, UK
Austria
Belgium
Finland
Faroe Island (Denmark)
France
Germany
Gibraltar, UK
Great Britain, UK
Iceland
Ireland
Isle of Man
Liechtenstein
Malta
Norway
Scotland
Spain
Sweden

North America (2)
Mohawk - Kahnawake
File Hills Band

Russia (1)
Kalmykia, Russia

South America (3)
Chaco, Argentina
Formosa, Argentina
Venezuela

Source: River City Group

Legislative and Regulatory Landscape

The policy issues posed by e-gambling are particularly acute. Governments and many ordinary people worry that turning the home PC and Internet enabled televisions and cellar phones into casinos and sports books will increase the prevalence of problem gambling and exacerbate its effects. Traditional land based casinos, lotteries, pari-mutuel sports and bookmakers see potentially vast new markets but, in the face of their continuing uncertain legality, are unsure how to enter them. Telecommunications and technology firms increasingly aware of Internet gambling's growing consumer base, are likewise intrigued but hesitant about getting involved with something that may prove embarrassing, or even criminal.

For regulators the issues posed by e-gambling's advent include all of the above plus one: the Internet invalidates the territorial nature of licensing. Though less immediate a public concern than potential increases in problem gambling, this is extremely important to regulators. *Licensure* is the legal basis for gambling. The power to grant, revoke or withhold licenses is a sovereign prerogative. Jurisdiction over licensee activity is co-terminous with

state, provincial and national borders; it follows that states have sovereign power over gambling activities within their borders.

Pre-Internet, it was not possible to supply demand for blackjack in, say, Nevada, without a Nevada gaming license. Exceptions to this practical limitation, gambling transactions readily transmitted through wires, were largely confined to betting on sports and racing; the slow evolution of wire communications technology permitted an orderly and effective modification of gambling law and regulation that accommodated these exceptions within the framework of sovereign national power. It all worked fairly well.

The Internet changes the licensing paradigm and with it the basis for gambling control. Borderless Internet markets invalidate the key assumption on which licensure depends. The Internet makes it eminently possible for someone to supply Nevada demand for blackjack from locations outside Nevada *without a license issued by the State of Nevada*--and, not incidentally, *without paying Nevada gambling privilege taxes*. Similar statements apply equally to other commercially significant games. This fact, already evident, poses problems for regulators with dimensions that are not yet wholly apparent.

The Factors Driving Internet Gambling

Internet gambling is in an early stage in what is certain to be a lengthy evolutionary process. What are the underlying factors that will govern the regulation of e-gambling, this new and (for governments) problematic thing under the sun?

The factors powering the development of Internet gambling include consumer demand; ease of entry and the arrival of name brands; product quality advantages; internal gambling industry pressures; Internet gambling's exceptional profitability and its consequent attractiveness to sources of investment capital; tax advantages, and the consumer price advantages created by low- or untaxed e-gambling businesses located in tax havens; the Internet's unique ability to facilitate communities of interacting individuals centered on shared interests or activities; and the enabling technology of the Internet itself.

Far from the simple phenomenon it is often assumed to be, online gambling is highly complex, rooted in the nature of the Internet itself and the still imperfectly understood psychological and emotional motivations for risking money at commercial games. Complex phenomena may not be amenable to simple policy solutions; less so, perhaps, when they are controversial.

Industries as diverse as recorded music and securities trading have already found that the market forces unleashed by the Internet are not controllable. For the music industry, particularly, which rests on intellectual property rights that are legally enforceable, e-commerce has been a traumatic learning experience. Courts and legislatures are proving to be poor vehicles to control the activities of consumers in cyberspace. For recorded music, and by extension for books, movies and any other intellectual property in digitized form, the massive shift of economic power from gatekeepers to consumers created by the Internet has created new policy issues. Law enforcement is the easy and emotionally satisfying answer for label executives unaccustomed to consumers listening to music without compensation to the record companies and artists. However, to date, law enforcement has not worked well.

Other policies and business models may be needed if content industries *as we know them* are to survive.

Gambling on the Internet raises similarly complex issues. A review of each of the identifiable drivers of growth in Internet gambling is, therefore, in order.

Consumer Demand
Prominent among the drivers of e-gambling growth is consumer demand. By 2004, websites offering gambling services will supply a global market of 15 million consumers who will spend $8.8 billion on blackjack, slot machines, sports betting, horse racing, lotteries and other commercial games.

The Internet is gambling's strongest growth market. As with other forms of e-commerce, PC wagering platforms are eclipsing older telephone systems, while interactive cable, now in its second go-around, is still trying to get out of the gate. In the United States, in spite of the proposed Internet Gambling Prohibition Act, a recent conviction of an off-shore sports book operator under the 1961 Wire Act, and the National Gambling Impact Study Commission's recommendation that Congress criminalize Internet gambling, market forces are overwhelming legislative and judicial efforts to halt the migration of gamblers to cyberspace. Internet gambling sites are multiplying like rabbits, and an increasing number of countries are legalizing this activity and bringing it under the control of regulatory régimes.

Tax Advantages
The Internet enables consumers who are so inclined to shop for price advantages created by low- or untaxed suppliers. This characteristic of e-commerce is calling sales taxes into question for a lengthening inventory of consumer goods: in a sense, the Internet is turning the globe into a borderless customs union. Long-term downward pressure on sales tax rates appears to be one consequence of the Internet revolution.

Consumer Pricing and Taxation
Like other consumers, many gamblers are price-sensitive. Sophisticated horse race and sports bettors are particularly sensitive to the consumer price of betting and are accustomed to seeking price advantages. Brand names and supplier reputations for integrity are important in all kinds of e-commerce. This is especially true for commercial gambling. If name brand operators enter the Internet market and offer value-driven gambling, many consumers may switch to the lower-priced service.

Falling consumer prices for forms of gambling offered by reputable Internet suppliers are likely to be another consequence of the growth of the e-gambling industry. In the United States, state-licensed casinos pay gaming privilege taxes ranging from effective rates of about 8% of win in Nevada and New Jersey to two and three times that amount in some riverboat states. Geography makes differential taxation feasible for land-based gaming. In cyberspace, differential taxation may not be feasible. If the U.K. betting levy experience is

any guide[8], downward pressure on tax rates for forms of gambling that develop major Internet supply in jurisdictions with low or no gambling privilege tax (and/or offer players shelter from income taxation) is going to be a long-term issue. Forecasting any other outcome from the current process is difficult.

Enabling Technology
The challenge that the Internet, with its borderless connectivity, poses for gambling regulation and control is that it invalidates the jurisdictional licenses that are the legal basis for existing gambling industries. A host of troublesome questions is thereby raised. Two of these questions are especially important: Do sovereign powers extend into cyberspace? Moreover, can national laws, particularly laws prohibiting Internet gambling, be enforced?

The Wire Act and Federal Prohibition

Press reports indicate that legislation that would criminalize Internet gambling may be reintroduced in upcoming legislative sessions. If one of these bills were to pass it would create a new Federal enforcement concern and, effectively, a new Federal jurisdiction: gambling in cyberspace.

Each of these bills has provoked considerable debate concerning enforceability. There is broad agreement that the Internet, by its nature, makes effective enforcement of prohibition exceedingly difficult.[9] The Lasseters Casino and World Sports Exchange examples presented later, reinforce this view, albeit in different ways.

Payment Mechanisms
The Unlawful Internet Gambling Funding Prohibition Act, or HR 556 is an attempt to prohibit Internet gambling by making it impossible for Americans to pay for their online gambling activities. This bill, like the Kyl legislation before it that attempted to block Internet gambling sites at the level of the Internet Service Provider (ISP), will be difficult to enforce. The first and most important component goes back to globalization. Take a look back at Exhibit 3. Gambling on the Internet is a sanctioned activity in a good proportion of the world. There are many banking institutions that are multinational- and many that are

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[8] In order to avoid paying a nine percent surcharge (that was passed on directly to consumers) a large number of major U.K. bookmaking concerns began to move their operations to offshore locations such as Alderney and the Isle of Man and service customers over the Internet tax-free. Faced with the prospect of decreasing tax revenue from the exodus, leaders in that country opted for law enforcement or the criminal code. They decided to lower the rate to a tax on profits rather than a surcharge. Following the announcement most of the major bookmakers announced their intention to move back on-shore.

[9] After a careful technological review, Australia's Productivity Commission came to a similar conclusion: "a policy of prohibiting access or provision *by Australians* [italics added] of online gaming is likely to be less enforceable than allowing some legal 'certified' sites", *Final Report* 18:55 ; "making it illegal to operate or use online gaming sites .... [by for example] blocking of notified illegal sites .... would have the likely effect of significantly reducing their use, albeit while also creating a black market" of illegal suppliers. p.18: 55. In light of these conclusions the Commission decided there are "good grounds for regulation of Internet gambling along lines appropriate for other gambling forms. The Commission considers that there are ways of sufficiently inhibiting access to (foreign-sourced) unlicensed sites to make such regulation effective. It would also be considered fair and be complied with by most consumers–whereas complete prohibition may not. Moreover, prohibition would eliminate some potential benefits from the technology (including competitive advantages in trade)."

based in other nations that have no U.S. contacts. It will be difficult for any U.S. legislation to prevent banks from participating in an entirely legal transaction on foreign soil.

That's the thing about globalization, it's a two way street. Money now flows across borders at a rapid rate, and if the U.S. wants the continuation of the inflows of foreign money and investment, it has to allow the outflows as well. In short, H.R. 566 can probably prevent Wells Fargo and Chase Manhattan from processing Internet gambling transactions. But it will be hard, if not impossible, to prevent an on-line gambler from depositing funds in U.K. or German bank that does.

The PayPal Problem

Now consider all the various companies that are actively courting on-line gambling companies with alternative payment mechanisms. A short list includes checking, ATM, debit and credit card transaction solutions--all available in a secure online environment. Some of these products authorize, process and manage electronic check transactions in an online environment; others enable operators to disburse customers' winnings or refunds through a funds transfer or automatic checking account debit and credit program.

These alternative solutions create easier ways to circumvent the proposed legislation: with third party processors, or the PayPal problem. PayPal is an e-commerce provider that allows individuals to establish a PayPal account by depositing funds. Users can use a credit card, check, or wire transfer. Once the account is established, Internet users can purchase goods and services from any site that utilizes the PayPal system--including eBay.com and gambling sites. If a foreign domiciled third-party processor like PayPal were to arise, it would be difficult for law enforcement to prevent funds from being deposited in these "non-gambling" accounts.

Is this level of enforcement sufficient to make prohibition good public policy? The answer depends partly on the policy goals that the supporters of prohibition seek to achieve. The question of what prohibition would accomplish goes to the heart of the debate over appropriate national policy for gambling. American history offers two experiences with prohibitory laws that provide insight into the likely consequences of adopting prohibition as policy for the phenomenon of Internet gambling. These, uniquely American, experiences are with alcohol and illegal sports betting.

The Prohibition of Alcohol in the United States

The 19th century Temperance Reform movement polarized the country over the issue of alcohol and in the aftermath of the Great War resulted in the 18th Amendment to the Constitution and the enforcing Volstead Act, passed in 1919.[10] The United States is the only

[10] Sixty-sixth Congress. Sess. I. Chap. 85. October 28, 1919.

Western country[11] to deal with the problematic aspects of alcohol by enforcing laws against its manufacture and sale. There is at least one good reason why. The so-called "Noble Experiment" failed, disastrously. Criminalizing drinking, a widely accepted behavior, created a vast market of thirsty consumers soon supplied by Al Capone and his unlettered but rapidly organizing associates .

While it may have been a moral triumph, as public policy, Prohibition was a catastrophe. The Volstead Act marked the intersection of a deadly combination: widespread demand for a good or service, in this case alcoholic beverages; ready supply through ease of transport (or an enabling technology) that cannot be effectively policed, in this case trucking; and prohibition.

An important assumption underlying the 18th Amendment and the Volstead Act was that Prohibition was enforceable. Its supporters promised that Prohibition would curtail the supply of alcoholic beverages and thereby reduce their consumption; ultimately it would eliminate drinking from American life. Despite vigorous enforcement, Prohibition failed to accomplish any of these goals. Instead of falling, consumption of alcoholic beverages *increased*, this rising demand, with its implied profitability, attracted suppliers undeterred by the fact that distilling and distributing liquor was a Federal crime. However unintended the result, Prohibition forcibly transferred ownership of the liquor industry from licensed, legitimate companies to organized crime. This was in fact the single outstanding accomplishment of the Volstead Act, for Prohibition, while it encouraged rather than discouraged criminals, operated effectively against legitimate business. Consumer protections were eliminated in the process; dangerous and even lethal alcoholic beverages moved through the illicit distribution system; alcohol blindness, and death, were direct consequences.

Enormous resources were allocated to enforcing the Volstead Act before it was repealed in 1933. Human nature refused to cooperate. Seventy years later America is still drinking; and still struggling with the harmful effects of alcohol. Drunk driving is an issue. Drinking by minors is an issue. Alcoholism is an issue. The Volstead Act did more damage to America than alcohol ever could, [12] but alcohol's social ills remain real, and persistent.

Sports Betting, the Wire Act, and the Professional Amateur Sports Protection Act

Bookmaking on the outcome of sports events is the object of the Wire Act. While American lottery, pari-mutuel, and casino prohibitions have been dismantled, the bookmaking

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[11] The *Qur'an* prohibits wine-drinking (though without imposing a penalty), an Arabic game of chance, *maysir*, and loaning money at interest as behaviors of the pagan Arab society that Muhammad sought to eradicate. Subsequent religious authorities strengthened and codified these prohibitions, and by the Middle Ages alcohol was forbidden to Moslems. Since thenalcohol, as well as gambling and (until recent times) loaning money at interest, have been generally proscribed in predominantly Islamic countries. *The Cambridge History of Islam*, vol. 2, pp. 54-542. London and New York: Cambridge University Press. 1970.

[12] A recent, accessible, non-scholarly summary of Prohibition's adverse impacts on American society is provided by Edward Behr, *Prohibition. Thirteen Years that Changed America.* New York: Arcade Publishing. Distributed by Little, Brown and Company. 1996.

prohibition remains firmly in place. Only Nevada has full-scale sports and race book operations.

The Federal Wire Act was enacted in 1961. Like the Volstead Act, Federal agents have enforced it sporadically; there have been numerous indictments and numerous convictions. Considerable law enforcement and judicial system resources have been absorbed by enforcement of the Wire Act. The Professional and Amateur Sports Protection Act that passed in February 1991 strengthened this legislation. This Act prohibits any State from authorizing any forms of sports wagering. It provides an exception only for those States that had existing authorized sports wagering. Effectively, the combination of the Wire Act and the Professional and Amateur Sports Protection Act made sports wagering illegal throughout the United States, with the exception of Nevada. But no one can argue that the Wire Act and the Sports Protection Act have eradicated illegal bookmaking or even made a dent in it.

Why? Because bookmaking lies at the same fatal intersection marked by the Volstead Act: widespread demand for a good or service (betting sports); ready supply through enabling technology that cannot be effectively policed (the telephone); and prohibition. Some of the persons prosecuted under the Wire Act could be classified as representatives of organized crime, and to the extent that the Wire Act has proven an effective weapon against that enemy, one can argue that it has served the public interest.

As social engineering, however, the Federal sports wagering prohibitions have proven as ineffective as the Volstead Act. They failed to discourage illicit bookmakers from supplying demand for sports betting, and failed to discourage this demand. Forty-one years after the enactment of the Wire Act, few if any law enforcement officers would subscribe to the statement that illegal betting on sports is not widespread in the United States. Three Federal study commissions [13] and countless investigating bodies have concluded that sports betting is pervasive and that bookmakers are readily available. Indeed, some believe that there may be little unsupplied demand for sports betting in the United States today, despite Federal prohibition.

What have the Federal sports wagering prohibitions actually accomplished? They have prevented legitimate business from supplying massive consumer demand for sports betting. In effect, they have ensured that ownership and operation of the U.S. bookmaking industry remains with the criminal entrepreneurs that the Wire Act has proven ineffective in eradicating. They also cast Federal law enforcement agencies in the role of regulators of the American sports betting market--a role for which they are poorly equipped.

This experience (like the earlier Volstead Act) says something important about prohibition as public policy. Criminal codes are tools for dealing with aberrant criminal behavior. They are poor tools for dealing with behavior in which many law-abiding citizens engage and that most law-abiding citizens do not consider crimes. That is the lesson of the American experience with the Volstead Act and the Federal sports wagering prohibitions. The implication is that trying to prohibit widely accepted activities or behaviors does not work, particularly when the prohibitory law is hard to enforce.

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[13] Commission on the Review of the National Policy Toward Gambling, 1975; Task Force on Organized Crime, 1967; The National Gambling Impact Study Commission, 1999.

The implication here is that prohibition may be a poor policy choice for Internet gambling. If the American experience with alcohol and sports betting is any guide, an Internet gambling prohibition may repeat the failures of the Volstead Act and the Federal sports wagering prohibitions, exacting a heavy price from legitimate gambling industries and the consuming public and contributing little in the way of concrete benefits in return. The elements of the failed "Noble Experiment" are again present: widespread demand (for Internet gambling); an enabling technology (the Internet) that cannot be effectively policed; licensed, legitimate suppliers in other countries that don't wish to subject their citizens to Noble Experiments and won't respect other nation's prohibitions.

The assumption that underlies the argument for prohibiting Internet gambling is that it will prevent gambling through the Internet because enforcement efforts will prevent demand for Internet gambling from being supplied. The American experience with bookmaking and the Federal prohibition suggests that this assumption is false. In so far as Internet gambling offers parallels with alcohol consumption and sports betting, its prohibition is likely to have similar results. It will not discourage or reduce demand for Internet gambling nor will it reduce problem gambling.

If nations around the world were to rise up and attempt to stamp out gambling on the Internet, prohibition could work. But that hasn't happened: nearly 55 nations to date have seen fit to authorize and regulate gambling on the Internet, and it looks like there will be many more to come. On a global Internet, it will be very difficult for one nation or even many nations to undue or circumvent the legal policies of another. Is this good thing? Maybe not, but it is the hard reality of the digital age.

The Option of Regulation

The second policy option is regulation in a legal context. Regulation would allow legitimate companies holding State gambling licenses to supply consumers with honest, regulated betting services that provide jobs and tax revenues. The various regulatory régimes that have evolved over the past half-century would continue their evolution in cyberspace, perhaps adding, as a necessary consequence of cyberspace's borderless nature, *reciprocity* in standards of integrity and uniform rates of taxation in this process.

Although not without difficulties, gambling on the Internet is regulatable. In fact, if policymakers and governments were to take a proactive approach to the regulation of Internet gambling, the world's most tightly regulated gambling market could thereby be created. In regulating gambling on the Internet, the possibilities offered by current and future technologies, are nearly limitless.

Competition among Jurisdictions

As with a prohibition, regulation of Internet gambling in one nation will have little effect on the actions of another. Unlike prohibition, however, regulation presents the gambling public with a choice, in this case between gambling over the Internet with an enterprise based in loosely regulated offshore tax havens or with recognized branded companies in major nations that can offer gamblers consumer protections.

Commerce on the Internet has developed along some very interesting lines that have direct relevance to the potential of regulating gambling on the Internet. Given its questionable legal status in some nations, e-gambling is certainly unique in the e-commerce world. But rather than excepting Internet gambling from the rules that govern commerce on the Internet, this uniqueness makes the industry more beholden to them. Two consumer demands, trust and security, currently dominate commerce on the Internet; this has manifold implications for e-gambling.

E-commerce companies have determined that the most effective method of dealing with issues of trust is branding. The relative successes of companies like eBay, Amazon.com and other Internet commerce companies, stand as testament to the potential of the Internet. The also provide evidence of the importance of branding in cyberspace. On the Internet, any company can market its products to a global audience. While this makes the market extremely competitive, branding has become a key component of success on the Internet because consumers are reluctant to give their credit card numbers to companies that they do not know and trust.

This has very positive implications for the regulation of gambling on the Internet. Although the policymakers in one nation do not have control of the actions of another, Internet gambling businesses operating in a tightly regulated environment have a large competitive advantage over those in less stringent locales. In short, it is our belief that the importance of regulation in consumer decision making matrixes will drive them to tightly regulated recognized gambling companies in great numbers.

In terms of the day-to-day regulation of gambling on the Internet, the fact that this business is conducted in a networked data-intensive environment offers opportunities for oversight in several critical areas.

1. **Operator Fitness:** The first stage in gambling regulation is licensure. For cyberspace gambling businesses, the process of background checks and assessments of fitness to hold an Internet gambling license could be achieved using the same methods as in traditional land based gaming.

2. **Technical Integrity and Game Fairness:** Front- and back-end software would undergo testing by regulatory agencies or companies in their employ. This would be very similar to the way that slot machines and their back-end systems undergo regulatory scrutiny today. The testing of random number generators and overall "game fairness" can follow previously constructed models for computer based gambling. Internet gambling operations will require another level of scrutiny, however, since the Internet gambling systems reside on the open Internet. Testing of overall site security will be required so that players and operators can be reasonably assured that their site is adequately protected from "hackers" and "crackers."

3. **Auditing and Oversight:** In terms of auditing and oversight, the conduct of commercial gambling games over a computer network has great advantages for regulators. Regulators can be given server level access to licensed gambling suppliers; this means that all aspects of the gambling operation, down to the level of

the amount bet by Player X at 12:03 p.m. on Saturday, July 15, 2000, can be scrutinized. Furthermore, since storage (hard drives) is inexpensive, this data can be maintained indefinitely. Entire gambling operations could be audited in a matter of seconds, and, with server-level access, regulators could "watch" gambling activity in progress.

4. **Prevention of minors or other undesirables:** Another important element in the regulation of commercial gambling is preventing children or other undesirables from gaining access to Internet gambling sites. Although arguably the weakest component of on-line gambling regulation[14], we believe that more than adequate results can be achieved by a number of alternative methods, many which could work in conjunction with each other. First, licensed Internet gambling companies can require that "off-line" proof of identity be provided to ascertain that a prospective player is who they say they are and is of appropriate age and fitness to gamble on the Internet. As further protection, regulations could require that gambling sites require all new customers to install and use specialized copies of commercially available filtering software such as "Net Nanny" or "Cyber Patrol" to prevent their children from accessing gambling sites. These methods could be combined with "IP Header Addressing" (sort of an Internet call tracing method) to block citizens from countries that have prohibited gambling on the Internet.

   No security is full proof, however, and there may be rare instances when children do gain access to Internet gambling sites, as they occasionally gain access to land-based casinos, purchase alcohol, and engage in other activity that society has attempted to shield them from. The standard applied to the Internet should be the same as in the "real world", imposing fines on operators that let minors or other desirables gain access, but with the understanding that these events will inevitably occur despite an operators best efforts, on-line and off-line.

5. **Customer Protections:** As with land based gambling, in the event of a dispute between operators and players, the same institutions and regulatory procedures should be applied to gambling on the Internet.

6. **Problem Gambling:** It is in the area of the unique negative externality of problem gambling that the Internet offers unsurpassed potential . The Internet is a data-intensive medium, and as we noted above with regard to auditing and oversight, every detail of every gambling transaction can be recorded and, potentially, analyzed in the Internet gambling environment. Players "chasing losses" or exhibiting other behaviors which are indicative of problem gambling can be flagged and their betting habits further analyzed. Internet gambling sites could be required to have information about problem gambling present on players' screens at all times. Licensed gambling sites could be required to have links to helplines and problem

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[14] The (not so) old saying goes "[that] on the Internet no one knows you're a dog." While this is certainly true, and has distinct implications for gambling regulation, it is important to recognize that this issue of proper and accurate identification of customers is a problem that faces many e-commerce businesses, the auction site eBay in particular. In other words, it seems very likely that in the very near future new and better methods will be developed by technology companies such as eBay, to accurately identify people on the Internet

gambling counselors. Furthermore, players should have the ability to set their own pre-determined betting limits and to exclude themselves from play.

7. **Taxation:** As with e-commerce generally, taxation of e-gambling is an extremely complex issue. While the vast majority of Internet gamblers will flock to Internet gambling businesses in tightly regulated jurisdictions, the Internet, by its very nature, is borderless. National or territorial governments have little or no influence on what goes on outside their jurisdiction. Most gambling privilege tax rates are inversely related to the amount of competition in the market. At the low end of the tax scale, places like Nevada do not restrict the number of licensees and the amount of supply in the market is determined wholly by how much gambling supply the market will bear. At the other end of the spectrum, places like Germany tax gambling revenues at extremely high rates in exchange for monopoly or quasi-monopoly status for their licensees. In other words, high gambling privilege taxes are usually predicated upon monopoly or quasi-monopoly supply.

   Individual governments cannot offer monopoly or quasi-monopoly status to Internet gambling licensees. The Internet is a global medium, and the behavior of the vast majority of consumers and operators is outside the control of any one government. In other words, rates of taxation that are at least not somewhat competitive (i.e. relatively low) with the (currently, and likely to remain) tax-free banana republics may undo the competitive advantage that is provided by offering Internet gambling from a recognized nation.

Even under an effective regulatory structure, the social concerns raised by the advent of gambling on the Internet would remain. Like alcoholic beverages, commercial gambling, whether location-based or on an individual's PC, is a problematic activity; while harmless for most consumers, it is dangerous for some. Like alcoholism, there is no easy solution to the tragedies of problem gambling. However, Internet gambling has the potential to teach us more about how problem gambling develops in individuals and could even help us create tools to combat it more effectively than ever before.

In preventing and/or treating problem gambling, prohibition is probably not the answer since pushing suppliers beyond the reach of regulators makes it harder, not easier, to protect consumers who are at risk. The foregoing list, while certainly not complete, is at least a step in the direction of policies that might help in the real world.

Congress and Offshore Operations

As a practical matter, what would prohibition accomplish? Particularly as it relates to offshore operations which are the beyond the reach of U.S. law. As an approach to this question, let us look at two historical examples:

Lasseters Casino

The United States has thus far been unable to prevent Australia's Northern Territory from licensing Lasseters Casino and permitting Lasseters, under the terms of this license, from accepting wagers placed in the United States regardless of the status of such gambling under

United States law. Lasseters has been doing exactly this since it opened its online casino in April 1999 without provoking a legal challenge from U.S. authorities. Short of negotiating a treaty or resorting to war against Australia, the United States appears to have no further recourse in acting against online gambling operations such as Lasseters.

World Sports Exchange

Now consider the somewhat analogous case of Jay Cohen, the president of World Sports Exchange, an Antigua-licensed, Antigua-based Internet and telephone betting service that also accepted wagers placed by persons in the United States. Mr. Cohen was swept up along with a number of similar Caribbean-based Internet and/or telephone betting services in a 7-month criminal investigation by Federal agents and prosecuted by Mary Jo White, U.S. Attorney for the Southern District of New York.[15] Believing himself innocent, Mr. Cohen voluntarily returned to the United States to stand trial. On February 28, 2000, a jury found him guilty of violating the Wire Act. Although the case is being appealed, it demonstrates that Federal enforcement agents can successfully prosecute offshore violators of the Wire Act if they are apprehended on U.S. soil.

But let us step out side the court room for a moment. As a practical matter what does the Cohen case really mean? First, Mr. Cohen **voluntary** returned to the United States to stand trial. If he had decided otherwise, he would probably still be drinking margaritas on the beach. Second, Mr. Cohen's company, World Sports Exchange, is still operating, and still taking bets from United States citizens.

While Jay Cohen's conviction establishes a precedent, it also demonstrates that *partial* enforcement of anti-Internet gambling laws is probably about as far as the Federal Government is going to get.[16] The allocation of massive law enforcement resources to investigating and prosecuting offshore infractions of the Wire Act does not seem to be in the cards.

The Consequences of Congressional Failure to Act

Formulating public policy is never easy, particularly when it relates to gambling. Unlike the hard sciences, nature has supplied no objectively "right" answers for policy makers, and to construct rational gambling policy, decisions must be based on the expected outcomes of given actions. To construct rational policy towards gambling on the Internet, or terrestrial gambling for that matter, accurate assessments of the benefits and costs of any given action can be immensely beneficial.

With relatively few exceptions, the power to authorize, endorse, and license gambling has been tacitly reserved by the States. It is a policy that allows the State of Utah to remain

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[15]Indictments returned March 4, 1998. Benjamin Weiser, "14 Facing Charges In First U.S. Action On Internet Betting", *The New York Times*, March 5, 1998.

[16]On September 16, 1999 Judge Wood of the United States District Court in the Southern District of New York (Manhattan) denied a motion to dismiss the indictment against Allen Ross, who was also named in the March 4, 1998 complaint filed by Mary Jo White against Caribbean Internet gambling operators. *UNITED STATES OF AMERICA* v. *Allen Ross*, No. 98 CR. 1174-1(KMV), Order, September 16, 1999, Wood, J. Judge Wood's construction of the Wire Act (18 U.S.C. § 1084(a)) in this Order is relevant.

gambling free, and Mississippi to implement economic redevelopment around riverboat casinos. While Senator Kyl and others have attempted to pass legislation prohibiting on-line gambling, many States have not waited for Congress to act. Currently five States, Illinois, Louisiana, Michigan, South Dakota, and Oregon have passed prohibitory legislation.[17] One State, Nevada has recently passed legislation that permits interactive gambling sites to operate from within the State. AB 466 was signed into law by Gov. Kenny Guinn June 14, 2001.[18]

It is our view that despite what if any action by Congress, gambling on the Internet and through other Interactive media will continue and thrive, despite considerable conflict along the way. In the end, we believe that licensed and regulated e-gambling is inevitable. It seems that one way or another prohibition will prove an unworkable policy, as the Volstead Act did before it. The industry will simply move underground, and it will continue to take bets from U.S. citizens. By taking this industry from the hands of licensed, regulated suppliers and handing it to criminals a Federal prohibition will likely do more harm than good.

Whether gambling is right or wrong, moral, or immoral is certainly debatable, whether it is pervasive is not. At the heart of the issue of gambling on the Internet, and gambling anywhere else for that matter, is the view that gambling is immoral, and is an example of the increasing decadence of our society. Maybe it is. Nevertheless, the fact remains that neither this view nor gambling, are going away.

Right or wrong, gambling like other "sin" products such as alcohol or tobacco does create some very discernable harms. Problem and pathological gambling are as real as gambling is ubiquitous, and greater efforts must be made to prevent it. One thing is certain, suppliers to an illegal U.S. gambling market will not be overly concerned about problem and pathological gambling and its impact upon our society.

At the end of the day, the reality of the Internet, the reality of consumer demand for commercial gambling games and the reality of the Cohen case and others like it will set in. It is hard to see any other outcome from the process now underway.

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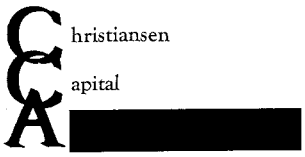
[17] It is important to note, however that in Oregon pari-mutuel horse racing was exempted from the ban and in Michigan the wording of the bill would appear to allow existing licensees to offer e-gambling to residents of Michigan, although this has yet to be tested.

[18] The original bill, AB 296, was eventually incorporated into a companion bill, AB 578. At first, the bill passed in both houses, yet failed at the final step. The legislation, however, was brought to back life when it was piggybacked unto AB 466, a bill that creates a uniform, statewide system for issuing work cards to gambling employees. The next step is for the Nevada Gaming Board and the Gaming Control Board to do an in-house survey of applicable legislation on the state and federal levels and develop rules and regulations.



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August 28, 2001

Ms. Sue Kelly
Chairwoman
Subcommittee on Oversight and Investigations
Committee on Financial Services
2129 Rayburn House Office Building
Washington D.C. 20515

Re: Financial Aspects of Internet Gambling: Good Gamble or Bad Bet?

Dear Chairwoman Kelly:

I respectfully submit the following response to your follow up questions regarding the July 12, 2001 hearing on Internet gambling, your questions are reprinted below in bold.

1. **"You acknowledge that preventing children from gambling is the "weakest component of on-line gambling regulation". Are you comfortable that the software that currently exists to monitor and deter such use is up to the task?"**

Your colleague Mr. Gutierrez asked a similar question so much of my response here replicates that answer. I am comfortable that the technology and non-technical processes exist today to prevent underage gambling as successfully as the off-line lotteries, casinos, and off-track betting parlors do. In fact, it is my belief that the level of unauthorized access could be substantially less than with traditional venues, with proper technology and procedures.

I refer to this particular aspect of e-gambling regulation as the weakest aspect of regulation, not because there are not effective alternatives, but more because there is currently no single good alternative as there is with problem gambling and geographic location technology.

The key to regulating gambling on the Internet is not a lack of tools to regulate, but in adopting technologies or processes to meet these guidelines that do not impose overly onerous requirements for consumers. Long detailed forms, hard-to-install hardware, and in-person verification may make on-line gambling unattractive to all but a few. In other words, the difficulty in regulating gambling on the Internet is in striking the correct balance between effective regulation and good business practices. It is in this unique area of preventing minors from accessing e-gambling sites that that balance will have to be skewed in favor of strong regulation that makes consumers jump through a few hoops.

The potential for underage gambling on the Internet is a very real problem and one that needs to be addressed responsibly by the regulators of gambling activity, and by policy makers. Legitimate regulatory authorities such as the Nevada Gaming Commission and the Gaming Review Board of the United

Kingdom are already studying this issue very carefully. It is the stated policy of both bodies that if adequate measures are not available to positively identify who e-gamblers are the activity (Internet gambling) should not be allowed.

But as stated in my written testimony, and referred to in your question above, positive identification is possible. A simple, yet effective, method is off-line proof of identity. In other words, in order to establish an account with a legally licensed e-gambling provider, customers must show up at a physical location and present two forms of picture identification.

"Off-line" proof of identity is very easy to implement and is currently used in 2 of the 10 states[1] that currently allow telephone and Internet betting on horse races. The leading downside of such a non-technical solution is to the gambling operator. The "hassle" of having to show up in person to open an account serves as an impediment to consumers. Used in conjunction with commercially available software such as NetNanny (that could be required to be installed on the account holders computer before that individual could play) would prove an extremely effective mechanism for positive identification of Internet gamblers.

It is important to put Internet gambling and regulation in the context of the wider industry that it is a part--traditional or "real world" gambling. It as an unfortunate, but undeniable fact, that occasionally underage individuals participate in gambling[2], state-run lotteries have been documented as having the highest incidence of underage play.[3] In the real world gambling operators (except state lotteries) are fined if someone underage is found to have gambled at their facility. If the operator does not take adequate measures to prevent underage gambling on its premises the operator could have their license revoked. This deterrent should extend to the Internet as well.

As already noted, off-line proof of identity is one possible effective and practical solution to the positive identification problem, but there are others as well. Much of the technology already exists to implement a series of technical and non-technical solutions that would certainly meet or exceed the current ability of off-line gambling operations (particularly the lotteries) to keep out minors, and are less onerous on legitimate consumers than in-person verification. We address the various issues of age verification by the classes of unauthorized access that may occur and the currently available solutions.

The first class is the unknown minor, the one who attempts to open an account themselves. If that minor holds a credit card and attempts to use that card to open an account, credit card processors already have the information required to develop an effective mechanism for preventing these individuals from accessing on-line gaming sites.

When issuing a card, financial institutions do their own due diligence on customers, crosschecking ages and social security numbers with credit reports. E-gambling providers could utilize that information to verify the age of the cardholder. Many e-commerce providers are already utilizing a variant of that system. If you go to Amazon.com, order a book, and enter in a phony shipping address, you will not be receiving your book. The system checks the shipping address entered in by on-line purchasers with that on file with the credit card company. If they do not match, Amazon does not ship--the same can be done with age information and e-gambling services.

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[1] Nevada and Ohio.

[2] As they also gain access to alcohol and tobacco products.

[3] Volberg, Rachel &W. Lamar Moore. 1999. Gambling and Problem Gambling among Washington State Adolescents: A Replication Study, 1993 to 1999. Olympia, WA: Washington State Lottery.

The last class is the would-be underage gambler that attempts to open an account with mom or dad's card; there are several methods of effectively preventing access of that kind, that become even more effective when utilized in tandem.

One such system performs a credit check on whomever is listed as attempting to open an account (in our example, junior's mother). The system reviews that credit report and compiles a series of questions from the information in the credit report such as, "who services your student loans?", and other questions (chosen at random) that would likely only be known by the rightful holder.

Some other non-technical solutions include provisions that account withdrawals can only be accomplished by means of a check made payable to the accountholder and sent to the address of the accountholder (or by means of an electronic transfer to a bank account held by the verified accountholder). Finally off-line redemption can be required, in other words the accountholder must withdraw funds from the wagering account at an approved facility by presenting verifiable personal and account identification information.

There also currently a host of technologies on the market that allow for positive identification of individuals. As I noted I my written testimony positive identification is a problem that extends far beyond gambling, and many forward thinking companies are developing effective solutions.

Some of the technology currently available on the market includes: biometric technology such as computer mice that do a fingerprint scan when used, retina-scanning technology available through a simple web cam that is as accurate as a fingerprint. There is no dearth of technology available today that can effectively address minor access to on-line gambling sites and the processes and technologies that I describe above are all available now. Furthermore, although I try to stay on top of these technologies as they are developed, I am probably not aware of them all, so better technology could exist.

The final prong of any age verification strategy is to require that filtering software be installed on all systems accessing gambling sites. This system is easy to implement, the gambling operator simply verifies that program is running on the clients computer before providing access to the gambling site, which prevents junior from gambling with his Dad's account.

In short, there are a multitude of ways in which minors and other undesirables can be effectively prevented from gambling on-line. Depending upon how aggressive policy makers wish to be with regard to the prevention of underage gambling, utilizing combinations and variations of the list of alternatives provided above, meaningfully regulated on-line gambling sites can exceed what has been done off-line in preventing the access of minors.

2. **"You make the case for regulating the Internet gambling industry rather that prohibiting it. However, Mr. Fahrenkopf, who represents the industry, has told us today that the technology is not available for Internet gambling regulation and enforcement. Do you agree with him that the technology to regulate the industry is not available? If so, does that make your recommendation moot?"**

With all do respect, Mr. Farenkopf and the industry he represents are not technologists and are hardly qualified to assess the availability or inavailability of any technology.

The truth of the matter is that the industry Mr. Farenkopf represents is divided about this new-fangled Internet thing. In an environment of uncertainty, many will seek the refuge of the status quo. To the

American casino industry, the Internet represents both opportunity and threat; and many haven't figured out which one it is yet. But if the process in Nevada continues (attempting to answer that very question—is Internet gambling regulatable?) I would be surprised if the American Gaming Association maintains its current position beyond 2002.

In short, the technology does exist to regulate Internet gambling. The technology exists to create the most highly regulated gambling market in the world. No, I do not agree with Mr. Farenkopf and the position of the AGA, and I suspect that a year from now, neither will they.

(3) "Even if Congress and the States developed a system for proper regulation of the domestic Internet gambling industry, wouldn't an unregulated – or poorly regulated – offshore industry continue?"

Yes, it probably will continue in a limited fashion by offering rebates to big bettors and significantly lowering the price of betting services. Furthermore, given the reality of American politics today bookmaking on the Internet, or otherwise, will not be legal outside the state of the Nevada. This will assure their continued existence. Over the past six years, illegal sports betting has moved from the corner bookie to the Caribbean, and it probably will not be coming back.

But the Caribbean industry would contract greatly from its current dimensions. The average consumer will always choose the regulated service over the unregulated one, if it is available to them. While there have been numerous studies off e-gamblers and e-commerce users in general that support this notion, a simple rational observation is much more descriptive. Think about it, would you be more likely to gamble at Casino-on-Net.com or Harrahs.com and MGMMirage.com?

Respectfully submitted,

/signed/

Sebastian Sinclair
Vice President
Christiansen Capital Advisors, LLC

Statement of Keith S. Whyte, Executive Director,
National Council on Problem Gambling

Internet Gambling

U.S. House of Representatives Committee on Financial Services,
Subcommittee on Oversight & Investigations

July 12, 2001

Statement of Keith Whyte, Executive Director of the National Council on Problem Gambling, on internet gambling before the U.S. House of Representatives Committee on Financial Services, Subcommittee on Oversight & Investigations

July 12, 2001

Chairman Kelly and members of the Committee on Financial Services, Subcommittee on Oversight and Investigations, thank you for the opportunity to testify before this committee on behalf of the National Council on Problem Gambling, the nation's oldest and largest organization dedicated to addressing problem gambling. Since 1972 the National Council on Problem Gambling (NCPG) has worked with Federal, state, tribal and local governments, industry and other non-profit groups on problem gambling issues. We have consistently maintained a position of neutrality, neither supporting nor opposing gambling.

The mission of the National Council on Problem Gambling is to increase public awareness of pathological gambling, ensure the widespread availability of treatment for problem gamblers and their families, and to encourage research and programs for prevention and education.

The National Council administers several nationwide programs, including a 24-hour confidential helpline, a gambling-specific certification program for treatment professionals, and sponsorship of the *Journal of Gambling Studies*, the only academic journal in the world devoted to problem gambling research. In addition, the NCPG sponsors regional, national and international conferences, supports research, distributes literature and works with other organizations involved in problem gambling issues. The National Council on Problem Gambling is a tax-exempt, non-profit corporation.

The NCPG currently has 33 state affiliate chapters, and corporate and individual members. They encompass the leading United States and international experts in problem gambling policy, research, prevention, education and treatment. We represent individuals, families and loved ones affected by problem and pathological gambling.

Pathological gambling is a mental disorder, classified under the American Psychiatric Association Diagnostic and Statistical Manual of Mental Disorders (DSM-IV). Approximately 1% (2.5 million) U.S. adults meet criteria for pathological gambling in a given year (attached). Another 2-3% (7.5 million) gamble in ways that cause harm to themselves and their families, and meet some criteria for pathological gambling. Altogether, an estimated 11 million Americans are directly suffering from gambling-related problems. High rates of financial debt, unemployment, bankruptcy, divorce homelessness, other mental health and substance abuse problems, and suicide are associated with problem gambling.

Gambling on the internet is a relatively new issue. A recently completed prevalence study in Oregon provides some updated data on internet gambling (Volberg

2001). Lifetime participation in Internet gambling increased from 0.3% in 1997 to 1.1% in 2000. Past year Internet gambling participation increased from 0.1% in 1997 to 0.7% in 2000. Both of these changes were statistically significant. Out of a total of 14 different activities, Internet gambling was the only one that saw an increase in participation among Oregon residents between 1997 and 2000. While Internet gambling participation rates are still low, the 260% increase in lifetime Internet gambling participation in Oregon corresponds to an estimated annual growth rate of approximately 54 percent. The six-fold increase (600%) in past year Internet gambling participation in Oregon corresponds to an estimated annual growth rate of more than 91 percent.

Although internet gambling has been growing rapidly, the overall rate of U.S. lifetime participation in all types of gambling has remained roughly stable at around 75-80% of the adult population over the past 20 years. Of course there have been changes in preference among the many different forms of gambling. Each form of gambling (church bingo, sports betting, casino roulette, etc…) has different structural characteristics. Internet gambling obviously provides heightened accessibility, and accessibility is a risk factor for developing gambling problems, although not the only factor. Gambling in social isolation and use of credit to gamble may also be additional risk factors. It is important to note that the structure of a game alone does not determine the development of a gambling problem. An individual's bio/psycho/social factors interact with the game and the environment in extremely complex ways that are not fully understood.

However, technology also provides potential to develop responsible gaming features on a site. Every patron is uniquely identified and every bet and transaction on a site is known. It is possible for discreet and targeted informational messages to be delivered via email to potential problem gamblers. Operational means of addressing problem gambling such as bet and deposit limits, credit checks and self exclusion programs could be researched, developed and implemented. However, it is important to realize that in spite of this potential, very few existing internet gambling operators have adopted even minimal standards to protect their customers.

A particular area of concern is the intersection of three broad trends among adolescents: 1) gambling participation and prevalence of problem gambling, 2) access to credit, and 3) access to the internet. Surveys show that past-year participation in gambling by adolescents is high: Non-Casino Card Games: 40%, Games of Skill: 32%, Sports Gambling: 31%, Lottery: 30%. A compilation of gambling prevalence surveys by Harvard Medical School (Shaffer, Hall & VanderBilt, 1997) that adolescents have generally double the rate of gambling problems of adults. These figures may in fact be underestimates, as all these activities are illegal for adolescents and the statistics are based on telephone interviews with adolescents at home.

Furthermore, youth have access to credit, through their parents or increasingly on their own. According to the Consumer Federation of America study (Manning, 1999), about 70 percent of undergraduates at four-year colleges possess at least one credit card. Internet access and usage among college students is widespread.

There are preliminary indications that individuals are developing problems with internet gambling. For example, roughly 2% of the intake calls to the NCPG national helpline (800.522.4700) cited internet gambling as their most problematic activity. I have attached a chart detailing 18 such calls from January through April 2001. I must stress that this small sample is not representative of our helpline, all problem gambling helplines or all problem gamblers. The National Research Council estimates that only 3% of problem gamblers seek help in a given year (NRC, 1999). Nevertheless, I hope it provides a face to our main concern—problem gamblers and their families.

Regardless of the well-intentioned debate this particular issue has generated, the fact remains that for most individuals with gambling problems there is no help available. Approximately 80% of insurance companies will not reimburse for a diagnosis of pathological gambling, and only 15 states provide even a minimal level of services for problem gamblers. Whether the problem gambler is a grandparent hooked on church bingo, an athlete addicted to the thrill of winning, a teacher obsessed with winning a multi-million dollar state lottery prize or a video poker player trying to cope with personal problems, their real difficulty is not finding avenues to gamble. Their real difficulty is finding the road to help and recovery.

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DIAGNOSTIC CRITERIA FOR 312.31 PATHOLOGICAL GAMBLING

A. Persistent and recurrent maladaptive gambling behavior as indicated by five (or more) of the following:

(1) is preoccupied with gambling (e.g., preoccupied with reliving past gambling experiences, handicapping or planning the next venture, or thinking of ways to get money with which to gamble)

(2) needs to gamble with increasing amounts of money in order to achieve the desired excitement

(3) has repeated unsuccessful efforts to control, cut back, or stop gambling

(4) is restless or irritable when attempting to cut down or stop gambling

(5) gambles as a way of escaping from problems or of relieving a dysphoric mood (e.g., feelings of helplessness, guilt, anxiety, depression)

(6) after losing money gambling, often returns another day to get even ("chasing" one's losses)

(7) lies to family members, therapist, or others to conceal the extent of involvement with gambling

(8) has committed illegal acts such as forgery, fraud, theft, or embezzlement to finance gambling

(9) has jeopardized or lost a significant relationship, job, or educational or career opportunity because of gambling

(10) relies on others to provide money to relieve a desperate financial situation caused by gambling

B. The gambling behavior is not better accounted for by a Manic Episode.

Selected Data from NCPG 800.522.4700 January-April 2001 Intakes
Only Callers Who Identified Interent Gambling As Their Primary Gambling P

Date	Gambler Age	Gambler Ethnicity	Gambler Gender	Marital Status	Gambler Employed	Gambler Occupation	State	Amount of Gambling Debt	
7-Jan	18-25	Asian American	Male	Single	Yes	Student	TX	Unsure	Caller is going to graduate soon, h
9-Jan	Unasked	Unasked	Male	Married	Unasked		KS	min.$10K,unsure	He stole a check that was for her, her. He's also taken all of her liqu
23-Jan	35-44	Unasked	Female	Married	No	Homemaker, disability	CO	Unsure	His wife has been spending all of t
29-Jan	35-44	Caucasian	Female	Married	Yes	Clean offices	CO	$20,001 - $30,000	Two hours ago she lost $20,000
30-Jan	18-25	Unasked	Male	Single	Yes	2 jobs& fulltime student	VA	Unsure	His son's grades had slipped, they omething was wrong.
31-Jan	18-25	Caucasian	Male	Separated	Yes	University work study	NC	$1,001 - $5,000	Lost $ 900 last night Internet gamb
2-Feb	35-44	Caucasian	Female	Married	Yes	Travel Agent	TX	$5,000.	"In the last 3 days I have lost $3,0
6-Feb	18-25	Caucasian	Male	Single.	Yes	.	PA	Unasked	Said he had gone to treatment pro
8-Feb	26-34	Caucasian	Male	Single	Yes	Computer Analyst	TX	$30,000	Caller was at the xxxxxx Casino a looked at the [problem gambling b
14-Feb	45-54	Asian American	Male	Married	Yes	Government Agency	TN	$80,000	" I just don't know what to do."
8-Mar	35-44	Caucasian	Female	Married	Yes	Self employed		$50,001 - $100,000	Promised husband she would quit
12-Mar	35-44	Caucasian	Female	Single	Yes	Buys & sells metals	IL	Unknown	Daughter s having money problem
21-Mar	35-44	Caucasian	Male	Married	Yes	Contractor	MD	$501 - $1000	Gambler is spending all of his sav
21-Mar	18-25	Caucasian	Male	Single	No	College student	TN	Unasked	Spending too much money and tim
25-Mar	26-34	Caucasian	Male	Married	No	Student	AR	$251 - $500	Lost a lot of money.
30-Mar	45-54	Unasked	Male	Married	Yes	Day trader	CO	Unsure	Sister wants to sell house, he will
16-Apr	35-44	Caucasian	Female	Married	Yes	Bar Waitress	TX	Unsure	The caller's wife has passed hot c
30-Apr	35-44	Caucasian	Female	Married	Yes	Attorney	PA	$50,001 - $100,000	The caller told her husband that sh gambling.

National Council on Problem Gambling
NATIONAL HELPLINE 1-800-522-4700 24 HOUR CONFIDENTIAL

August 14, 2001

Janice Zanardi
Committee on Banking & Financial Services
2129 Rayburn House Office Building
Washington, DC 20515

Dear Janice:

Thank you for the chance to respond to additional questions regarding the July 12, 2001 hearing by Subcommittee on Oversight & Investigations on internet gambling. I have answered the specific questions below.

1) Education on problem gambling is not widespread. In this regard, problem gambling lags far behind substance abuse and mental health. For example, to my knowledge there are only two states (Massachusetts and Louisiana) that require problem gambling be addressed as part of the high school curriculum. In informal surveys and conversations with college coaches, teachers and administrators, I have found that most universities do not even have a policy on gambling by students and most student health centers do not screen for gambling problems. This is particularly striking in light of the evidence, as I indicated in my written testimony, that the rate of problem gambling for youth is double that of adults. Further, I have attached a fact sheet on youth and adolescent gambling for further reference. Regarding efforts by colleges to provide education, the National Collegiate Athletic Association is concerned primarily with the integrity of the game, and has developed materials to that end. Although research shows that student-athletes have higher rates of problem gambling than the general student population, these materials do meaningfully address problem gambling among student-athletes.
2) The low rate of help seeking by problem gamblers is likely a result of several factors, including: 1) failure of health insurance to reimburse for treatment for pathological gamblers; 2) failure of most states to provide treatment services; 3) unwillingness of problem gamblers to seek treatment, especially if it involves stopping gambling, 4) stigma and lack of awareness among public that problem gambling is a mental health disorder and that treatment may be effective. It is important to remember the "Gamblers Fallacy": that the next bet may be a winner and solve all your problems. Therefore, the only way out seems to be to bet more, and the only sure way to "lose" is not to play. This downward spiral is reinforced by the occasional large win and the inability of the problem gambler to stop gambling.
3) One innovative program was developed jointly by Global Cash Access and NCPG. It is called the Self Transaction Exclusion Program (STEP), which allows cardholders to fill out a form (copy attached) to deactivate their credit cards at all GCA machines in gaming locations across the nation. This program is combined with placement of a

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http://www.ncpgambling.org

tollfree 24hr problem gambling helpline on all GCA ATM's and cash advance machines and on the back of approximately 40 million receipts generated by the machines. I do not know if this program, or a similar concept, would be applicable to help credit card companies.

4) As the internet gaming industry is largely located outside of the US, they have shown little desire to work with NCPG. Several internet casinos link to our website, and this allows their visitors to access our site, with its resources for problem gamblers, including our online directory of nationally certified gambling counselors. We have also developed a written policy that we do not endorse or approve of these sites, even though they may choose to link to us.
5) There are a number of programs that internet gaming operators could put in place, including betting limits, "cooling off periods", consistent and accurate enforcement of minimum legal age, and resources for problem gamblers built into or linked to the site. Obviously, these are broad categories, and each would have to be elaborated upon to produce an adequate safeguard. I have attached a "Social Responsibility Checklist" that expand on these categories from GamCare, our counterpart in the United Kingdom.

However, the underlying principle for addressing problem gambling, whether online or among bingo, lottery, casino or sports gamblers, is prevention and education. We have learned from our experience with alcohol and other drugs that the most effective means of addressing these issues is from the public health perspective. By investing in broad based prevention for youth, education on risks and odds for those that gamble, and having adequate treatment as a last resort, we can meaningfully reduce the enormous but hidden social costs of this issue. The National Gambling Impact Study Commission estimated the aggregate annual costs of problem gambling at $5 billion.

The Federal Government is only just beginning to address problem gambling. To date, the National Institute of Health has dedicated $9 million in basic research funding, and the Center for Mental Health Services has awarded an $85,000 contract for basic studies. To date, no other Federal agency has addressed this issue. I hope to work with members of Congress to devote more resources and to develop a broad range of partnerships on this issue. By working together, we can make a difference.

Thank you for the opportunity to testify before the House Financial Services Committee, and for the chance to follow-up on questions posed by Rep. Guiterrez. I would be happy to respond to any additional questions from the Committee.

Sincerely,

Keith Whyte
Executive Director
National Council on Problem Gambling

Cc: Rep. Gutierrez

National Council on Problem Gambling

Adolescent Gambling and Problem Gambling Fact Sheet

The U.S. National Gambling Impact Study Commission recently concluded: "One of the most troubling aspects of problem and pathological gambling is its prevalence among youth and adolescents."

In the US and throughout the world, many people begin gambling as children. For example:

- In a study of British adolescents ages 13 and 14, the mean age of initiation into gambling for social recreation or entertainment was found to be 8.3 years for boys and 8.9 years for girls (Ide-Smith and Lea, 1988).
- Wynne (1996) found that 48% of juvenile problem gamblers had an age of onset before 10 years of age.
- In a study of Minnesota youth, 60% of high school students who are problem gamblers had gambled in the 6th grade or before. There were no problem gamblers among those who first gambled in the 12th grade (Winters, 1990).
- Jacobs (2000) reports that juvenile involvement in gambling in the U.S. now exceeds the expected onset for their use of cigarettes, hard liquor and marijuana.

> "Preliminary evidence suggests that the earlier people begin gambling, the more likely they are to experience problems from gambling."— U.S. National Research Council, p. 140

Gambling Participation Among Youth

Children routinely gamble. Although the private card games and wagering on games of skill are the most popular forms of gambling for youth, gambling on sporting events and the lottery are also very popular.

- Approximately 80% of youth age 12 to 17 have gambled in the last 12 months (Gupta, 2000).
- In his meta-analysis, Shaffer (1998) determined the top four average adolescent gambling prevalence rates for the last 12 months: Non-Casino Card Games: 40%, Games of Skill: 32%, Sports Gambling: 31%, Lottery: 30%.

> "If my life was a tree, one branch would be that I'm a thief, another branch is that I'm a liar, another being that I'm no longer in school, and another being that I no longer have my parents trust and respect, and I'm not permitted to live in their home. But if you cut off each of the branches you still haven't gotten to the root of the problem which is my gambling."— Anonymous adolescent

Prevelance of Problems

Youth consistently show elevated rates of problem and pathological gambling compared to adults in the general population. Studies demonstrate that youth with gambling problems have family, academic, peer and legal problems.

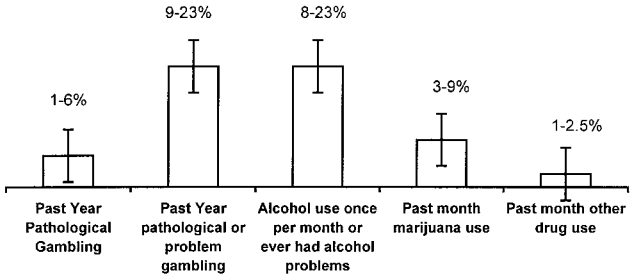
- A review of recent studies suggests between 9-14% of youth are classified as "at-risk" for a gambling problem, and 4-7% exhibit criteria of pathological gambling (Derevensky, 2000).
- Several studies have shown adolescent pathological gambling is associated with alcohol and drug use, truancy, low grades, problematic gambling in parents, and illegal activities to finance gambling (NGISC, 1999).
- Youth whose parents gambled excessively had twice the number of problems with the law and twice the attempted suicide rate than their classmates (Jacobs, 1989).
- Louisiana adolescents in juvenile detention are roughly 4 times as likely to have a serious gambling problem as their peers (Westphal, 1998).

Fact: In a recent review of 14 U.S. and 6 Canadian adolescent gambling studies, Jacobs found that in the past 10 years the number of teenagers ages 12 to 17 reporting serious gambling problems has increased by 50%, from 10 to 15 percent. The age of onset for gambling has dropped so that now, throughout America, the majority of 12-year-olds have already gambled (Jacobs, 2000).

Problem Gambling is a Serious Problem Similar to Substance Abuse

The data also clearly show that problem gambling is a serious issue, on par with or exceeding other well-recognized public health threats such as alcohol, marijuana and other drug use.

Gambling, Alcohol Use, and Drug Use Among Adolescents



Source: NRC, p. 94

Where to go for help:

The National Council on Problem Gambling and its 35 state affiliates offer a variety of services for problem gamblers and their loved ones.
Call the 24 hour, toll-free, National Problem Gambling Helpline:
(800.522.4700)
for confidential assistance. Resources are also available through the NCPG website:
www.ncpgambling.org

Primary references:
National Academy of Sciences, National Research Council, *Pathological Gambling: A Critical Review* (1999).
National Gambling Impact Study Commission, *Final Report* (1999).
*Additional references available on request.

INSTRUCTION TO REJECT CASH ADVANCE / ATM TRANSACTIONS
STEP (Self Transaction Exclusion Program)

The undersigned holder ("Cardholder") of the card specified below (the "Card") does hereby instruct Global Cash Access, L.L.C., a Delaware limited liability company ("GCA"), to reject any cash advance transaction requested using the Card. Cardholder is making this instruction pursuant to the Self Transaction Exclusion Program (STEP) initiative of GCA's Responsible Gaming Program and understands that this instruction may only be revoked using the written form of revocation set forth below. This instruction shall become effective upon GCA entering the Card into its computer systems as a card subject to a STEP instruction and shall remain in effect until GCA removes the Card from its computer systems as a card subject to a STEP instruction following GCA's receipt of a written revocation of such instruction using the form attached hereto.

Cardholder represents and warrants to GCA that Cardholder has all right, power and authority to make this instruction on behalf of all joint holders of the Card. Cardholder agrees that GCA's acceptance of this instruction would be solely as an accommodation to Cardholder, without any consideration to GCA; therefore, in no event shall GCA bear any liability for its acceptance, rejection, compliance or non-compliance with this instruction or any revocation thereof for any reason whatsoever. Cardholder hereby waives any claims against GCA in connection with this instruction or any revocation thereof, including without limitation GCA's rejection of transactions pursuant to this instruction, GCA's failure to comply with this instruction or GCA's rejection of transactions prior to the effectiveness of any revocation of this instruction, and Cardholder agrees to indemnify GCA against any liability arising from or relating to this instruction or any revocation thereof, including, without limitation, any liability to any joint holders of the Card, any liability to VISA U.S.A., Inc., MasterCard International, Inc., or Discover/Novus Inc, any liability to the issuer of the Card, and any liability to any acquiring or merchant bank involved in the processing of transactions involving the Card.

Cardholder agrees that this instruction and any revocation thereof shall be governed in all respects by the laws of the State of California, without regard to any conflicts of laws provisions which may result in the application of the laws of any jurisdiction other than the internal law other the State of California. Cardholder agrees that any claim or controversy arising out of this instruction or any revocation thereof shall be settled by final and binding arbitration under the Commercial Arbitration Rules of the American Arbitration Association in Santa Clara County in the State of California by three arbitrators, one of whom shall be selected by GCA, one of whom shall be selected by Cardholder and the third of whom shall be selected by the mutual agreement of the other two arbitrators. Judgment on any award rendered by the arbitrators may be entered in any federal or state court located in Santa Clara County in the State of California. The arbitrators shall award to the prevailing party, if any, as determined by the arbitrators, all costs, fees and expenses of such arbitration, including attorneys' fees.

Cardholder:_____

(Signature)_____ (Print Name)_____

Card Number:_____

Card Type: (check one) VISA ____ MasterCard ____ Discover____ Debit Card____ ATM ____

Requested Information (not required)

Address: _____

Phone: _____ Fax:_____

Mail the completed form to Global Cash Access, L.L.C., Attn: Cheryl Dotson 2350 Mission College Blvd. Suite 275 Santa Clara, CA 95054, or Fax to (408) 588-7145.

This information will remain confidential, and will be used only for the sole purpose intended. One form per card is required.

Should you have questions about the status of your instruction, please call Cheryl Dotson at 408-588-7155 ext. 14.

ONLINE GAMBLING
SOCIAL RESPONSIBILITY CHECKLIST

The following list is not exhaustive but represents the ground rules we would see as important regarding an online gambling site. A number of points are equally applicable to terrestrial operations.

1. There needs to be a system built into debit and credit card transactions that proves an effective check on age.

2. Advertising and promotional material should not target those under 18, should be honest, fair and give a balanced message with regard to winning and losing.

3. In addition to credit worthiness checks on account holders, limits should be placed on how much they can commit. This can either be a financial limit per session or per day.

4. There should be references to the need to keep gambling under control (i.e. a risks of the game message) that is a cautionary note rather than a health warning – and these should be sited where they will be read.

5. The homepage should carry the logo of the preferred social responsibility partner (hopefully GamCare) and a statement as to why the company is supportive of the partnership. (The latter does not have to be on the homepage). This notice should be accompanied with a link to the website of the preferred social responsibility partner.

6. A notice to where a gambler who is concerned with their own, or someone else's gambling can get help should appear at least twice. Once prominently mentioned in the text of the site, and alongside the menu box on the page where an online customer transfers money into their gambling account.

7. Whilst it is good commercial practice to promote products and provide the customer with information, there should be no encouragement to either re-invest winnings or chase losses. Gamblers should not be enticed to play on, the decision must be their own.

8. All gambling opportunities, but especially the rapid and interactive games should have a pause built in at predetermined intervals allowing the gambler to reflect on their desire to continue or withdraw. This is particularly important for those who may find it more difficult to stick to self-imposed limits.

9. Customers should have the opportunity to self-exclude themselves from an Internet gambling site. A system that enables them to do this should be in place, and clearly explained. Any self-exclusion scheme should be easy to carry out, and run for at least 6 months.

10. Any free practice mode that is offered to the customer must have an appropriate message regarding responsible gambling. We recommend that access to practice modes is prevented for those under the legal age to gamble. Giving access to such simulators could encourage someone underage to seek opportunities to gamble for real money.

11. Company staff, particularly senior management and customer support personnel should be trained/made aware of the importance of social impact issues and that there is no conflict between a company policy that maximises opportunity and minimises harm.

12 The company adopts a culture and practice that is able to demonstrate, and believe in, a socially responsible approach.

13. The site should be attractive enough to encourage online gamblers to use it in preference to those sites that are less well regulated or which are not committed to social responsibility.

14. The company commits itself to supporting organisations that provide treatment, training and education for problem gamblers, those at risk, and young gamblers.

15. Before launching a new product or developing an existing one the company consults, commercially in confidence, with the lead body involved with the social impact of gambling.

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Valerie C. Lorenz, Ph.D.
Executive Director
President of the Board

Kenneth J. Martz, Ph.D.
Clinical Director

Testimony by Valerie C. Lorenz, Ph.D.
Subcommittee on Oversight and Investigations
House Committee on Financial Services
U.S. House of Representatives
Washington, D.C.
July 12, 2001

Honorable Members of the Committee:

I have specializedin the field of compulsive gambling for almost thirty years. During that time I have seen gambling expand from the casinos of Las Vegas to casinos on riverboats and on Indian reservations, and now on the Internet. I have seen state lotteries expand across the nation, from a fifty-cent Pick 3 and Pick 4 ticket, with a once a day drawing, to as much as 20 scratch-off tickets on any given day, to $10 tickets, subscriptions, and keno, with advertisements featuring slots, horse races, and kiddie games. The casino industry for the past several years has taken a strong approach to developing a younger player market. We have indeed become a nation of gamblers, an industry that was promulgated by the casino industry and by governments.

One fact is clear and indisputable – no matter how much legalized gambling there is in this country, for the casino industry, "enough is never enough." The same can be said for state governments, which have come to depend in large part on lottery revenues Now these two giants want to go into the Internet business. Our own Congressional National Gambling Impact Study Commission clearly recommended "Put a moratorium on the expansion of gambling." Wouldn't it seem reasonable to listen to your own Congressional colleagues?

I have been asked to address four questions:

1. What impact has the Internet had on the problem of underage and pathological gambling? An interesting and important question. Let me respond: How much money has Congress allocated to such research – or to community education, treatment and prevention programs? It is difficult to answer your question with hard data; however, I

can tell you that in the 30 years that I have worked in this field, as legalized gambling of any form expanded, so did the number of gambling addicts. A Congressional study found in 1976 that less than one percent (.07%) of the adult population had gambling problems. And at that time, only Nevada had widespread gambling. Compulsive gambling among teenager, low income players, females and senior citizen gambler simply did not exist or if they did, did not step forward for treatment, because there wasn't any. Today, the estimates of compulsive gamblers ranges from 1.5% of the adult population to over 5%, depending on the amount of legal gambling in that state. Add to this, the even greater number of problem gamblers, those who abuse gambling and are on the verge of becoming addicted gamblers. The two groups of major increase – and concern – are our teenagers, and our senior citizens, both targets of the gaming industry.

What is the impact of compulsive gambling? Like alcoholism, gambling addiction, it will continue its spread into future generations. That is the nature of addictions. Compulsive gambling leads to financial ruin and severe indebtedness, with an increase in bankruptcies; broken families and lost homes; poor work productivity and terminations; health problems and addictions among the gamblers and their families; a frightening suicide rate; crimes which once were of a non-violent, financial nature, and which now have expanded to crimes of violence, including homicides.

We have a larger population of senior citizens than we have ever had before in our country. Usually on a monthly basis these seniors would take a bus to casinos or buy lottery tickets at their grocery stores. Now are we proposing that they stay at home and gamble over their TV or computers? They can lose everything they have ever worked for, and now they can lose it in their own living rooms, with no chance of financial recovery, or in many cases, survival. Isn't it responsible to rethink that proposal?

For the first time in our country we also have an entire generation growing up with government's message that it is OK to gamble, buy your lottery ticket and become a millionaire. This group of young people have been schooled on computers, many have their own laptops. Today they can log onto AOL, pull up Pogo, where of the half of the 40 choices are gambling games. Click on Poppit, a balloon game, or Sweet Tooth, trying to match three candies in a row, and every five minutes or so the player is given 30 or more seconds of casino advertisements. Ironically, Yahoo does not allow tobacco advertising, but what are the restrictions on gambling advertising? None. And just as the casinos entice their customers through freebies and comps, so do these Internet casinos – free gifts of $15, or $50, or $100, to get the player interested – and hooked.. It is so easy to forget the time spent on a computer, or to not realize how much money has been charged to a credit card. Both are tools of Internet gambling.

According to the Internet Gaming Council, a trade association, it has tracked 1,400 Web sites that invite people to gamble. Legal Internet gambling would dramatically increase these numbers.

"In 1999, gaming analysts estimated the Internet gambling industry brought in almost $1.2 billion. In 2001, that number shot to $3.1 billion. By 2003, expert say it will reach $6.3 billion" (Andi Atwater, the News Press, 7/8/2001).

Can you imagine what these figures will be with legalized Internet gambling? This is money that is gambled and lost by American citizens. When is enough, enough?

2. What technical and legal obstacles stand in the way of these issues? I would suggest that the lack of funds, the lack of legislation, and the lack of conceren or social conscience stand in the was of addressing these problems of compulsive gambling and future gambling addicts. Add to that the influence of the gambling industry, the casino industry which seems to pride itself on the political influence it has bought, through campaign contributions, advertising and lobbying.

Regulation? There is no way to regulate gambling on the Internet on one's computer or television. How can that possibly be done? "It's just not feasible for law enforcement to monitor what people are doing in their living rooms with their computers," said John Glogau, Special Counsel to Florida Attorney General Bob Butterworth. Does this country really want citizens who can gamble away their savings on Cybernet? The reality is, gambling on the Internet cannot be regulated. Consider existing conditions: No matter how many laws, policies, and procedures exist, teenagers can still get into casinos, get credit cards, and can gamble – just like they can get cigarettes and alcohol.

Can payments of wins be received if the Internet is legalized and if such name brand casinos like Caesar's and the Mirage control the market? Most likely. But on the other hand, how many players win? And how much do compulsive gamblers lose? And the little bit – or a lot of verbiage the Internet may put out concerning compulsive gambling, what good is that if there are no prevention or treatment programs?

3. What steps has the National Council on Problem Gambling taken, to date, to curb the abuses associated with Internet gambling? I don't know. I resigned from the National Council, in disgust, many years ago. I do know, however, that although it claims to take no stand, pro or con gambling, its President and members have publicly stated that they are not against increased gambling, as long as new gambling is accompanied with funds for compulsive gambling. Interesting. So is the fact that Paul Satre, CEO of Harrah's casinos, has been a Board member for many years.

I also know that for the past several years the casino industry has supported National Council conferences. A considerable segment of this year's National Council conference was related to casino industry issues. I know that Keith Whyte, its director, who formerly worked for the American Gaming Association (AGA), and who serves as Director of the National Council, received at least two years of salary from the AGA. It is my understanding that the National Council receives approximately 25% of its income from the casino industry.

4 What recommendations do you have for this Committee on steps Federal and State authorities should take to address Internet Gambling? First of all, as recommended by the National Gambling Impact Study Commission, put a moratorium on all expansion of legalized gambling, including Internet gambling. I would suggest a moratorium of at least ten years. Pass laws to make Internet gambling illegal, and enforce them. Make the fines large enough, and with imprisonment, so that illegal implementation of Internet gambling is not worth it.

Let state governments take a solid stance against expansion of gambling, particularly Internet gambling. A simple question should suffice: "Why should state governments encourage gambling that would compete with their own state lotteries?

I further recommend that both state governments and Congress address all issues and public policy relative to legalized gambling and compulsive gambling. Recognize and support the escalation of gambling addicts, with its devastating impact, through funding, top level administrative support, just as it has done with Alcoholism and Drug Addic-tion. Fights compulsive gambling, don't condone it or expand it. Protect the health and welfare of your citizens, that is what voters want from their elected officials. They did not vote for greed or poor health and a damaged community.

I thank you for permitting me to address you, and am prepared to respond to your questions.

Valerie C. Lorenz, Ph.D.

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Valerie C. Lorenz, Ph.D.
Executive Director
President of the Board

Harbour Center
Residential & Outpatient
Treatment Program

August 4, 2001

Mr. Hugh Nathanial Halpern
U.S. House of Representatives
Committee on Financial Services
2129 Rayburn House Office Building
Washington, DC 20515

Dear Mr. Halpern:

I have been asked by Congressman Luis Gutierrez to respond to two questions:

1.) In your opinion, what more can organizations aimed at helping compulsive or gambling addicts be doing for them?

Response: There are several groups which are working directly with gambling addicts; unfortunately, they tend to work independently of one another, thus the potential for better outcome is diminished. This pattern can be reversed with commitment, ethical standards and adequate funding.

Among these groups are The National Council on Problem Gambling, Gamblers Anonymous, National Coalition Against Gambling Expansion, Hotlines, AGA, treatment providers, gaming industry, Congress, state governments, and insurance companies.

National Council on Problem Gambling and its State Affiliates

The National Council on Problem Gambling could be the leader in efforts to address issues regarding compulsive gambling. That is its mission. It is my impression, though, that the National Council on Problem Gambling has veered off its course of neutrality, by way of its close association with the casino industry and its failure to interact similarly with those interest groups opposing gambling or the expansion of legalization of gambling.

The National Council needs funds to accomplish its mission. Currently, it is supported in part by the gaming industry, primarily casinos. The National Council could pursue funding from charitable foundations focusing on national health concerns.

The Compulsive Gambling Center, Inc., is a Not-for-Profit 501©3 tax-exempt agency.
Contributions are tax deductible.

This has a dual benefit – National Council would secure its own funding and increase its potential for funding from other charitable foundations funding health programs. This would secure its own funding while helping its state affiliates and other not-for-profits in the compulsive gambling field.

The National Council's efforts appear to be contained within its own organization and affiliates. Historically it has excluded, or worked competitively, with others helping compulsive gamblers. The National Council could broaden its service base to other not-for-profits and work more cooperatively with them.

The National Council might expend more effort in national issues, such as an amendment to the Americans With Disabilities Act, which specifically excludes compulsive gambling. It could be in active support of various recommendations made by the Congressional National Gambling Impact Study Commission.

State affiliates of National Council might limit their activities within their own geographic boundaries rather than competing with state affiliates or not-for-profits in other states.

Compulsive Gambling Hotlines

Currently several compulsive gambling hotlines provide information and referral services. These Hotline may be state funded, others are privately funded. Some are operated by the National Council and its state affiliates, others by treatment providers or independent contractors. There is no uniform method of data collection from calls. Each Hotline has its own intake form, most of which are incompatible with others except on a very minimal level, such as number of calls and length of calls. A tremendous amount of data, useful for governmental bodies, funding sources, researchers, educators and treatment providers is lost. This could be corrected if the various Hotlines were to agree on a universal intake form.

The Hotlines have inconsistent policies regarding referrals. Some hotlines refer only, or primarily, to Gamblers Anonymous. Others refer also to treatment providers; however, these referrals tend to be arbitrary, thus giving rise to unnecessary conflicts, competition, and questionable service, at the callers' and providers' expense.

A uniform referral list needs to be compiled. Each state-funded Hotline could mail out a complete list of referrals of treatment programs. This is not a difficult task, since less than a dozen residential treatment programs exist in the country. Each state or publicly funded Hotline should be required to make up a complete list of providers and treatment resources and adhere to fair standards.

It would seem expedient to coordinate all compulsive gambling Hotlines through a central body, such as a separate national Hotline. Currently there are two such major Hotlines, the 1-800-GAMBLER Hotline, established and operated by the Council on Problem Gambling of New Jersey over a dozen years ago, and the National Council's

Hotline. A new, totally separate, Congressionally funded national Hotline, providing crisis counseling, information and referral, on a 24-hour pay day basis, is recommended. This "U.S." Hotline could provide leadership, coordinate all Hotlines and their referral resources, reduce duplication of efforts and costs, could provide improved and timely assistance, and discourage unfair or inefficient practices of other Hotlines. Most importantly, it could establish a comprehensive intake form and start gathering data from throughout the country.

The New Jersey Council's 800-GAMBLER number is highly visible, especially for visitors to Atlantic City. It is mandated by New Jersey law to be printed on all gambling advertisements and in gambling venues, such as casinos and race tracks. This same approach could be used to promote the "U.S." Hotline.

The "U.S." Hotline could make referrals to all compulsive gambling hotlines, and not limit its referrals to state affiliates of the National Council as is current practice. For instance, a call from Maryland to the 800-GAMBLER Hotline is referred to the National Council's Hotline. National Council transfers calls to the Texas Council on Problem Gambling Hotline. The Texas Council has its own unique system of referrals to providers, its written materials sent to callers is limited, it does not keep current information on Maryland's resources, and does not have an intake form comparable with other Hotlines.

A new pattern of reduced number of calls to Hotlines has emerged in the past two years or so. One explanation for this may be that potential callers are finding information on compulsive gambling and treatment programs on the Internet. We have seen this reversal at the Compulsive Gambling Center, and it confirmed by the Council on Problem Gambling of New Jersey. Another possible explanation for this is that state budget cuts have reduced advertising of Hotline services. In Iowa, for instance, the gambling assistance program "this year has a budget of $1.6 million, nearly $500,000 less than in the past fiscal year" (Des Moines Register, 7/4/01). That being the case, it might be prudent for Hotline researchers to include e-mail contacts in their data collection and reports..

It is further suggested that all Hotlines give out e-mail addresses and/or web sites of gambling assistance programs. Adding links on websites to other web sites could be highly responsive to those in need of help or information.

Compulsive Gambling Treatment Programs

Similarly, the various treatment programs could do more for their patients and other compulsive gamblers by developing a standard patient intake form which would allow for easy collection of research data of specific variables, such as demographics of the patient, dissociative disorder symptoms, family history of addiction, and complete diagnostic impression, rather than being limited simply to Pathological Gambling.

Idealistically, all treatment providers for compulsive gamblers would unite and share residential and outpatient treatment and program information. This would have to be on a voluntary basis, but has the potential for improving treatment and outcome, while being cost-effective.

Gamblers Anonymous

Gamblers Anonymous is a fellowship of compulsive gamblers. Its philosophy is to grow though attraction of its message, and not through public stands. Gamblers Anonymous has a 97% attrition rate, and there are few long-term members who would be willing to "go public." Its members, however, could speak up as individuals, rather than as members of Gamblers Anonymous.

The International Service Office of Gamblers Anonymous and individual chapters have participated in research studies. This cooperation could be encouraged, without violating member confidentiality, by GA members of state affiliates of National Council and by peer counselors participating in professional treatment for compulsive gamblers; thus data from Gamblers Anonymous, Hotlines, e-mails, and professional treatment providers could be included in a broader data base.

All Concerned Not-for-Profit Agencies

All not-for-profit groups dedicated to helping compulsive gamblers could assist in efforts to increase awareness and education of this illness. This could be done through public service announcements on radio and television, in newspapers and magazines, on billboards. The funding requirements are minimal, because not-for-profits have access to public service announcement free of charge. Not-for-profits could increase education and awareness by giving talks to community groups, churches, schools, business, banking and financial institutions, and industry. This is necessary to maintain not-for-profit status.

Similarly, these groups, or individual members of these groups, could monitor and counter the prolific and unethical gambling industry advertising, such as is seen in state lotteries, casinos and race tracks, and more recently on the Internet. It is virtually impossible to avoid exposure to gambling advertisements directed at minors, the elderly, and for personal pleasure or gain, and promoting the "quick fix." Their messages convey that having money, lots of money, is the ultimate goal in life, rather than education, work, family and community. Steps could be taken to press for their removal, particularly the state lottery advertising, which additionally promotes all other forms of gambling.

State Legislatures

State legislators are lobbied constantly by the gambling industry, such as the casinos, race track, and video gambling machine operations. These one-sided legislative solicitations could be countered if legislators and their staff were to demand equal time for opposing or neutral groups. Legislation might be a first step in setting a limit on the amount of time and money spent on lobbying for their causes by the gambling industry.

Illegal gambling, especially sports betting, is widespread in each state. Legal gambling exists in 47 states. The impact of compulsive gambling is statewide and national in scope. Legislators pass gambling bills to "keep the money in our state." Might state legislators and other policy makers look not only at the financial benefits of gambling, but also at the prevalence, financial costs and social costs of compulsive gambling? It is something they can ask of the numerous task forces they form.

State General Funds receive millions of dollars from gambling. State legislators might consider spending some of that money on compulsive gambling assistance.

A number of state legislatures have established state offices and allocate varying amounts of funds. These state offices need to expand in the future to enlarge the scope of their authority, responsibilities, and services. Historically gambling assistance funds have been reduced over the years (Iowa, Maryland, and Texas are blatant examples). These state gambling officials must prevent or reverse this trend, if they are to be able to counteract the growth and socio-economic impact of compulsive gambling.

Congressional Studies

The recent Congressional National Gambling Impact Study Commission devoted an entire chapter in its Final Report to gambling addiction, and made recommendations on this growing national health problem. One of the recommendations was to put a moratorium on all further expansion of gambling. It also addressed the issues of Internet gambling. Congress should pass legislation to implement some of the Commission's recommendations. Importantly, future Commissions need more authority and power.

Congress and Other Federal Offices

Congress and various committees have shown an increasing interest in compulsive gambling. In my opinion it is essential that Congress establish a governmental Office on Gambling, an Ombudsman on compulsive gambling, and an Advisory Board to conduct ongoing studies of public policy on gambling and the impact of compulsive gambling, similarly to proposed state legislative efforts. Congress might find it useful to have a "Gambling Czar." A comparison may be made – Congress set up an office of Drug Czar, but Congress did not legalize drugs. In contrast, gambling was expanded by Congress, yet there is no equivalent to the "Drug Czar."

Military studies indicate a widespread prevalence of gambling, debts, and suicides in all branches of the Armed Forces. The House Armed Services Committee and its Senate counterpart need to pass legislation to include "and compulsive gambling" in its U.S. Code which refers to alcohol and drug addiction treatment.

Further, Congress could require military researchers to include gambling addiction, debts, crime and suicides among military members and their dependents in these studies.

Treatment programs, such as the Brecksville (Ohio) VA Medical Center and at Camp Pendleton, could be established on military bases in the US and out-of-country. The same applies to Veterans Administration Medical Centers.

The *Army Times*, *Navy Times* and other military publications have written about compulsive gambling. The publications provide a cost-effective vehicle for education, prevention, and referrals. These newspapers could be encouraged to do more.

Further, Congress must require the Surgeon Generals' Office to acknowledge that compulsive gambling has become a national health problem, and tate action, specifically in exploring co-morbidity, resulting medical illness and complications, and suicides.

Casino Industry

In recent years the casino industry has stated its concern about compulsive gambling, and its leaders insist that compulsive gamblers are bad for business. That being the case, the casino industry needs to be proactive and forceful in self-exclusion policies. New Jersey interest groups were able to force a mandate that casinos offer a life-time exclusion service. The casinos were opting for a one-year self-exclusion policy.

The casinos and other gambling venues can improve employee health insurance Currently most health insurances of casino (and race track) employees is limited.

The casino industry is targeting "a younger player" and seniors. If the casino industry is truly concerned about compulsive gambling, then it needs to close its day care centers for guests of their casinos. Further, casinos could discontinue a policy of permitting minors, and toddlers, to enter any casino. State laws could require this off-limits to minors (age 21) policy, in order to keep licenses in effect.

Since casinos affirm their concern about youth and gambling, then they might consider removing the themed slots which have emerged in recent years. A sample of these themes are Scabble, Yahtzee, the Addams Family, Austin Powers, Dream of Jeannie, and Wheel of Fortune, to name just a few.

Many compulsive gamblers started gambling in early teen years. In recent years the casino industry has participated in job fairs at junior high schools, promoting the benefits of casino employment. This is inconsistent with its stated concern about compulsive gambling and youth.

Again, casinos' concern about compulsive gambling needs to be more visible. All casino advertising and stationary could have a statement about gambling addiction on it. Signage at casinos must be large and prominently displayed. A warning sticker about gambling addiction could be put on every slot machine, and at every card or dice table and roulette wheel.

Seniors are particularly vulnerable to onset of gambling addiction in late years, for many reasons: retirement, death of a spouse, loneliness, poor health. Aggressive programs, such as Station Casino's 55+ Club, invitations to special events, discount coupons, etc., may reinforce a vulnerability, and lead to addiction. These promotions may need to be reconsidered in view of the casinos' public concern about senior gambling addiction.

Senior Centers, AARP and Offices on Aging

These groups have started warning seniors about the addictiveness of gambling. The Joslyn Senior Center (Palm Spring, CA) recently hosted a seminar on gambling addiction among retirees. Other groups are campaigning to warn seniors of excessive gambling. In Florida last month, compulsive gambling specialists started a think tank, and the Office on Aging in California held its first conference on this issue. All of these efforts could be duplicated throughout the country. AARP and state Offices on Aging might be the initiators of this education and prevention direction.

American Gaming Association

It is my understanding that the American Gaming Association (AGA) represents the Nevada casino industry, and not all casinos, such as tribal casinos, and not all gaming. The AGA actively extols its concern about compulsive gambling, yet it promotes the concept of "responsible gaming." The two are mutually exclusive. By clinical definition Pathological Gambling is no longer "responsible" and is, in fact, out-of-control, addicted gambling. For the sake of accuracy and credibility, the AGA might reconsider its posture and promote one concept, rather than blending the two, inaccurately.

Put in another way, "responsible gaming" promotes gambling, whereas compulsive gambling treatment philosophy by professionals and Gamblers Anonymous is abstinence from gambling. In spite of recent comments made by the former vice president of the National Council on Problem Gambling, there is no empirical research evidence that compulsive gamblers can reverse their addiction to being "controlled" gamblers or "responsible" gamblers. "Harm reduction" is effective with heavy social gamblers, not with compulsive gamblers. This is a belief espoused by the gaming industry, again geared to seniors. Perhaps the AGA should fund long-term research on this hypothesis of "responsible gamming" and "harm reduction" in gambling addicts.

The AGA perhaps could spend more effort in understanding the contributing factors to developing pathological gambling, such as wide-spread gambling. It needs to learn that knowing the odds of a bet or symptoms of the addiction holds no meaning for the compulsive gambler who "chases" losses and is "in denial." The AGA must recognize that the ability or failure to self-diagnose does not then result in being able to seek treatment, what little is available; wanting treatment when such exposure may lead to stigma or loss of job; or having the funds to pay for treatment.

The AGA could study the process of addiction, thus recognizing that self-medicating through short-term attempts at abstinence results in relapse and more extensive gambling, the psychology of compulsive gambling, the competitive nature of the compulsive gambler and gambling for the sake of beating the odds.

The AGA might want to review its marketing and its funding, objectively, and then follow a more accurate and ethical course based on statements of concern about compulsive gambling.

National Center for Responsible Gaming

Funding research by the gaming industry on compulsive gambling is suspect from the onset, due to possible hidden agendas. This is historically true of all research on one's own products or services. One such highly-funded National Center for Responsible Gaming researcher coined the phrase "disordered" gambling. This has no clinical value, nor community acceptance. Again, "responsible gaming" and "harm reduction" apply to heavy gamblers or temporarily abusive gamblers, and not to compulsive gamblers. The Center's goals and objectives need to be reviewed, if it is to gain respect and its research be accepted in the clinical arena. Research on non-compulsive gambling would be a more responsible agenda and its findings could be helpful to the gaming industry.

Anti-Gambling or Gambling Expansion Group

Anti-gambling groups have been and will continue to lobby for a moratorium on expansion of gambling; their concerns are about quality of life for all citizens. They are concerned about the financial and social costs of gambling. They have great concern about compulsive gambling and they educate their communities about this illness. They are more focused on a moratorium on gambling rather than funding for research, treatment programs, and training of treatment providers. They themselves have limited funds, thus a focus on its messages must be balanced with their efforts to increase financial support for their own groups, in order to expand and espouse their views..

Health Insurance Companies

Managed Care was conceived in an effort towards cost containment and prevention of unnecessary medical and mental health procedures. In response, it has developed its own definitions of "medical necessity" and standards of care. Denials for treatment and other abuses are commonplace. Appeals processes are taken to several levels, taking up clinical and administrative staff time and result in extra costs, while adding stress to the patient. This is particularly true with compulsive gamblers in treatment. Perhaps Secretaries of state health departments, Public Health Advocates, mental health association leaders and the U.S. Surgeon General could mediate with the insurance companies and improve the process of certification and reimbursement. Insurance and Managed Care companies might want to consider in-depth training on compulsive gambling for their caseworkers and supervisors.

2.) In your opinion, what can credit card companies be doing to help reduce the risk and problem of Internet gambling addiction?

Response: Credit card companies operate for profit. They, like the gaming industry, focus on developing a younger customer base for Internet gambling, cash advances, and purchases. These credit card solicitations can be found throughout the Internet, and college students routinely receive multiple applications per year. Students who are on limited budgets and often unfamiliar and inexperienced in money management are easy targets for credit cards, instant spending, and running up debts.

Students also have easy access to computers and the Internet. This gambling depends on payment through credit cards. Easy credit cards and Internet enticements to gamble reinforce a hallmark of compulsive gambling: the impulsive "quick fix" for money, due to the high costs of tuition, books, and housing.

One solution is obvious – do not permit the use of credit cards by anyone under the age of twenty-one (21). This could be done by very simple computer programming by credit card companies, which would automatically reject and deny applications to anyone under the age of twenty-one. To expect credit card companies to voluntarily implement such a standard is doubtful. It would require legislative action, with severe sanctions against these companies for any violation.

Credit card companies could suspend future applications from minors who attempt or are successful in circumventing the minimum age law. This could be for a designated time frame, but may also take legislative mandate to implement such a policy.

They could be required to print a simple statement on the front of each credit card billing statement or on the envelope itself. This would alert parents to prevent them from giving their minor children credit cards or allowing them to use an adult's credit card.

Credit card companies could monitor credit card charges from gambling sites. They now contact credit card holders if any unusual activity appears on an account, such as excessive purchases of a similar nature, i.e. jewelry, or repeated requests for a credit line increase. If this principle is applied to Internet gambling charges, such as sports betting or casino gambling, the risks of problem gambling could be reduced.

Compulsive gamblers often apply for a quantity of credit cards in their desperation for money. These requests are routinely monitored by credit card companies, thus the credit card companies could deny granting excessive numbers of credit cards. These companies might want to reconsider giving credit cards to non-working holders.

An alternative is to eliminate all Internet solicitation for credit cards, particularly if these solicitations are in any way associated with gambling.

Summary

In summation, there are many more things that could be done by organizations aimed at helping compulsive or gambling addicts. These organizations are not limited to the few not-for-profit problem gambling councils, the AGA and the Center for Responsible Gaming, but also include state legislatures and Congress, the gambling industry, especially casinos, insurance companies, and other for-profit or not-for-profit agencies. Theses efforts need to be supported by funding, commitment to common goals, and ethical standards.

The above suggestions are those which quickly come to mind, without the benefit of a team discussion. Some suggestions are too idealistic, given current practices and the lack of regulation. Perhaps, though, they may plant the seeds for other alternatives to be reviewed, which could combat the growth and devastation of compulsive gambling.

I thank you for including my opinions in your deliberations.

Valerie C. Lorenz, Ph.D.
Executive Director
Compulsive Gambling Center, Inc.

Testimony of Frank J. Fahrenkopf, Jr.
President and CEO
American Gaming Association
Before the House Financial Services Committee
July 12, 2001

Mr. Chairman, distinguished members of the committee, thank you for inviting me to testify today about the American Gaming Association's position on Internet gambling.

I am Frank J. Fahrenkopf, Jr., president and CEO of the American Gaming Association (AGA). The AGA is the national trade association of commercial casino companies, gaming equipment manufacturers, and other vendor-suppliers to the gaming industry. The association acts as a national clearinghouse for information about commercial casinos and as an advocate on federal and national issues for those it represents, including tens of millions of employees, patrons and shareholders. Other trade associations represent Native American casinos, the lotteries, the pari-mutuel industry, and other legal gaming entities. Our members are the companies with household names such as Harrah's, MGM MIRAGE and Park Place Entertainment. They operate land-based and riverboat casinos in 11 states across the country.

On behalf of the AGA, I appreciate this opportunity to address the topic of Internet gaming given the spread of e-commerce generally, the rapid rise in the number of Internet gambling sites and the concern that unregulated offshore Internet gaming sites now in operation circumvent state laws.

Some (particularly those now in the business of taking bets and wagers over the Internet or those with libertarian political views) argue that Internet gambling is no different from other forms of electronic commerce and that prohibition is impossible. However, consideration of questions about Internet gambling must be viewed in light of the nature of gaming and how decisions about public policy issues concerning legal wagering have been handled since the founding of the country and should continue to be resolved going forward.

As even the National Gambling Impact Study Commission reaffirmed in its final report in 1999, except for certain limited areas such as Internet gambling and Native American gaming, states (not the federal government) should decide whether to permit legal wagers by persons within their states, and if so, how to license those in the wagering business and how to tax and regulate their operations.

As we know, different states have decidedly different policies toward legal gambling, even among states that permit the same general type of legal wagering. For example, while all but three states (Hawaii, Tennessee, and Utah) have some form of legal wagering, and, as I indicated earlier, only 11 states have authorized commercial casinos and only one state has legal wagering on sports (other than horse and dog racing). Thus, unlike the use of the Internet to purchase a book, make a travel reservation, or even buy or sell stocks and bonds — all of which are legal transactions in each of the 50 states — the same is not true for each of the various forms of legal wagering.

As a result, our major concern with Internet gambling as it exists today is that it allows offshore of Web sites that accept bets and wagers to frustrate important state policies, including restrictions on the availability of gaming within each state. Similarly, unregulated Internet gambling that exists today allows an unlicensed, untaxed, unsupervised operator to engage in wagering that is otherwise subject to stringent federal and state regulatory controls. These controls are vital to preserving the honesty, integrity and fairness that those in the gaming industry today have worked so hard for so long to bring about.

According to published reports, confirmed by the casual use of any Internet search engine or the review of many publications catering to gaming patrons, there are over a thousand Web sites that accept bets and wagers, even from U.S. residents in states where such wagering is illegal. To the best of my knowledge, the most popular are, first, those that accept bets and wagers on the outcome of sporting events, and second, those that offer so-called cyber versions of casino-style games, such as slot machines, blackjack, craps and baccarat.

Sports betting is probably the most popular form of Internet gambling because unlike casino-style games over the Internet, the correct outcome of the wager can be determined by an independent event, namely the publicly available score of the game. However, the Internet allows U.S. citizens to place bets on sporting events in all 50 states, the District of Columbia, and U.S possessions, even though Congress banned such wagering in the Professional and Amateur Sports Protection Act of 1992 (except in states such as Nevada, where sports wagering was expressly grandfathered, as it was already legal and carefully regulated at the time of the 1992 Act.)

Even in the 11 states where commercial casinos are legal, they are not permitted to operate without prior state approval, including exhaustive background checks on major investors and key personnel. Some states do the same for major vendor-suppliers. Each state with commercial casinos considers their operation to be a privilege and not a matter of right. Most states with commercial casinos only permit them in certain designated counties or other geographically limited areas, often by decisions of local voters in a referendum. Thus, New Jersey has commercial casinos, but only in Atlantic City. Mississippi has commercial casinos, but only in those counties where it has been approved by voters, such as near Tunica in northwest Mississippi or along the state's Gulf Coast. Some states do not limit the number of licenses within those areas where casinos are legal, such as Mississippi, while others such as Illinois, Indiana and Louisiana have a statewide cap on the number of commercial casino licenses to be issued.

As with sports wagering, the existence of the Internet in its present form permits wagers to be placed outside of those areas where state and local decision makers have made it legal to do so. In addition to allowing players to place bets and wagers outside of the bounds of state limitations, the Internet at present allows persons to engage in the business of taking bets and wagers without complying with the extensive licensing and operational regulations imposed by states to protect the public and the integrity of the games.

The importance of this concern cannot be overstated. As the U.S. Department of Justice has stated before the U.S. Congress on several occasions, the law should treat physical world activity

and cyber activity over the Internet in the same manner, whether when it comes to gambling or otherwise. As the Department pointed out to the Senate Indian Affairs Committee on June 9, 1999, "If activity is prohibited in the physical world but not on the Internet, the Internet will become a safe haven for that criminal activity." Accordingly, the Justice Department has joined the National Association of Attorneys General in supporting efforts to amend federal gambling statutes to ensure that emerging technologies are not allowed to make legal in the cyber world what is already illegal if conducted over the telephone or in person at the corner tavern.

In addition to state-level restrictions on where legal wagering may take place, and extensive licensure and regulation of those who may engage in the business of taking legal wagers, there are important federal requirements applicable to commercial casinos and other forms of legal wagering. For example, U.S. commercial casinos are subject to federal corporate taxation, publicly traded companies comply with financial disclosure and other Securities and Exchange Commission rules, casinos file information reports on larger winnings with the IRS and withhold federal taxes on certain winnings, and casinos adhere to anti-money laundering statutes and regulations administered by the U.S. Treasury Department's Financial Crimes Enforcement Network. By contrast, those engaged in the business of illegal Internet wagering in the U.S. from offshore are not subject to U.S. law enforcement jurisdiction on these important matters of public administration.

There are those who claim that, even taking all of the above to be true, there is nothing that can be done to prevent the circumvention of federal and state law by offshore Internet gambling sites. However, this is not the first time that technology has threatened to allow persons to evade and avoid federal deference to state choices about the availability of legal wagering and how it is conducted. With respect to the telephone, the Wire Communications Act has been on the books since the early 1960s to prevent the use of the wires by a person in the business of betting or wagering to place or receive bets or wagers, or to transmit information assisting in the placing of such bets or wagers.

The previous U.S. Justice Department believed that "much of Internet gambling is already prohibited under existing laws," including the Wire Act. However, the statute as written in 1961 could be interpreted as applying only to sports wagering, calling into question its applicability to other types of wagers, and by its terms only to the use of a "wire communication facility." While most Internet transmissions presently use a "wire communication facility" at one or more steps along the way, the emerging technology of satellite transmissions and other interactive technologies might be interpreted as operating outside of the "wire communication facility" covered by existing law. Thus, ever since legislation to amend the Wire Communications Act in response to the Internet was first introduced in 1995, its sponsors have argued that it is merely designed to update federal statutes to preserve the same federal "back stop" of state decisions about legal wagering that has existed for decades.

In addition to a conflict between Internet gambling as we know it today and the traditional and well-founded approach of state regulation of legal wagering, it is important not to lose sight of why states that have legalized wagering have elected to do so. There are compelling positive economic benefits from various forms of legal wagering, including commercial casinos. This conclusion is also shared by the final report of the National Gambling Impact Study Commission

and the independent research it has produced, including a report by Professor Adam Rose of Penn State University on the economic impacts of legal gambling.

However, unlike the highly capital-intensive and labor-intensive forms of wagering in the physical world, such as those associated with casinos and pari-mutuel facilities, Internet gambling sites are very low in both capital investment and on-going demand for labor. Similarly, all forms of legal wagering produce significant tax revenues to federal, state and local governments for important public purposes, such as education, community development and benefits to special populations such as the elderly.

At this point, let me hasten to add that, despite the best efforts of some to argue the contrary, the commercial casino industry is not concerned about Internet gambling because we are worried about the supposed competition from Internet gambling sites. First, were Internet gambling to be made legal, the well-branded casino companies would be well-positioned to garner the major share of the market. Second, and perhaps more important in today's world, there is no comparison between the social-oriented, group-oriented entertainment experience of visiting a casino resort and the solitary experience of placing a bet or wager using a personal computer. Third, today's casino entertainment experience is about much more than legal wagering opportunities: whether measured by how people spend their time or how they spend their dollars, guests of U.S. commercial casinos are increasingly attracted as much or more by restaurants, shows, retail, recreation, and other non-gaming amenities. The fact that Internet gambling is not a competitive threat to U.S. commercial casinos is publicly shared by financial analysts at major Wall Street firms, whose job it is to analyze the competitive impact of market developments on the industries and firms they cover, including the major publicly-traded gaming companies AGA represents.

While the American Gaming Association could support appropriately drafted legislation to update federal statutes to preserve the traditional policy of state regulation, it is important to define key terms to be certain that we are all on the same song sheet as to what is meant by "Internet gambling." As discussed in this statement, "Internet gambling" refers to the use of the World Wide Web and other technologies by businesses to engage in wagering.

By contrast, new technologies, some involving the Internet and others involving non-Internet interactive computers, are in use or will soon be in use by licensed, regulated, legal gaming companies within the jurisdictions where they are permitted to operate under federal and state law. Examples include common pool wagering (where pari-mutuel wagers are pooled between a casino or other off-track betting facility and the track where the race is physically conducted); interactive computer systems; and the use of the World Wide Web to advertise and promote casino resort locations, including the taking of reservations for rooms and shows, without the use of the Internet for betting or wagering. Additional examples include new technology to facilitate and actually safeguard the operation of intrastate account wagering on sporting events.

In short, any changes to federal or state laws in the pursuit of making "Internet gambling" illegal, need not and should not be drawn so broadly as to lump the use of technology within otherwise legal limits in the same prohibited status as those who are doing so outside state law. This position is consistent with the policy of the Wire Communications Act, which, since the 1960s,

permits the use of the wires for wagers and information assisting in the placing of wagers where the transactions are entirely intrastate or between states in which the wagering in question is legal.

In other words, there is a difference between using technology to circumvent federal and state restrictions and regulations (as is done today by those operating offshore Internet gambling sites) and the use of technology by licensed operators to more efficiently deliver their services where, to whom, and under what conditions they are authorized by federal and state law to do so.

There are clearly understandable enforcement concerns, just as there are with most pieces of federal legislation that attempt to address the potential activities of millions of people. However, at this juncture, the choice is between sanctioning illegal Internet gambling by default, or carefully crafting amendments to update the Wire Act to prevent the circumvention of federal and state regulation of gaming activities. The latter course will allow state and local governments to retain their right to set policy and enforce state law for gaming activities by persons within their boundaries, both those in the business of betting and wagering, and for the protection of those individuals who choose to place bets or wagers.

When properly regulated, casino gaming and other forms of legal wagering are an enjoyable entertainment option for the vast majority of the American people. However, we know from the colorful history of wagering in America, from the lotteries of the last century to the operation of casinos before they were taken over by publicly held companies in this century, that unregulated, illegal wagering, if left unchecked, will lead to fraud and abuse given the sums of money involved. The Internet is a new and exciting vehicle, as was the telephone before it, but we lose sight of the importance of well-regulated gaming, supervised at the state level, at our peril.

The commercial casino industry's position on this issue has become somewhat obscured in recent months with the passage of Internet gambling legislation by the state of Nevada. Headlines in *The New York Times*, which said "Nevada Legalizes Internet Gambling," not only misrepresented our industry's position, but also misrepresented the content of the Nevada bill. I'd like to take a few minutes and explain to you what, in fact, this legislation does. The legislation authorizes the Nevada Gaming Commission, the state body that sets regulatory policy, to promulgate regulations IF — and that's a big IF — certain conditions can be met: 1) The state must be in compliance with all federal laws; 2) There must be an effective way to restrict access to those under age 21; 3) There must be an effective way to restrict access to only those residing in jurisdictions that permit Internet gambling; and 4) It must be determined that Internet gambling promotes the general welfare of the state.

The legislation also establishes a licensing framework similar to the stringent requirements already in place to acquire a casino operators' license. Only existing Nevada licensees will be eligible to become licensed Internet gambling operators. There are other requirements, depending on the location of the establishment within the state, that require existing licensees to have either a resort-hotel, a certain number of rooms or seats or have held a license for at least five years. Each licensee would be required to pay a fee of $500,000 for the first two years, in addition to a renewal fee of $250,000 a year. In addition, each operator would be required to pay a 6.25 percent tax on gross gaming revenue. The same licensing requirements would apply to

equipment manufacturers and suppliers. Any operators who create a site without the proper license will be subject to felony prosecution.

While they're not spelled out in the legislation, other factors will be considered by the Nevada Gaming Commission to provide additional safeguards for customers who might not be able to gamble responsibly. The commission will ensure self-exclusion for individuals who want to prevent their access. It will also establish betting limits and time limits that would apply to not just one site but across all Nevada Internet gambling sites.

These requirements make what Nevada is exploring very different from what is currently being conducted by offshore operators. As Brian Sandoval, chairman of the Nevada Gaming Commission, said, "This is not going to be the Oklahoma Rush" — although some Internet gambling supporters were hoping that would be the case. As stated explicitly in the legislation, Nevada is not seeking in any way to defy the federal government. In the coming months, after a thorough legal analysis, the Nevada Gaming Commission will be seeking a meeting with the U.S. attorney general to discuss the legality of Internet gambling as set forth by this legislation.

With 1,800 sites worldwide, generating between $3 billion and $4 billion annually, Internet gambling is growing by leaps and bounds. But this illegal activity remains largely unregulated. As the world leader in the gaming industry, Nevada believes it has the responsibility to step forward and act to determine what current and future regulatory actions might be taken regarding Internet gambling.

The AGA's role, meanwhile, is to keep our members informed of the latest developments on Internet gambling as a means of setting the association's policies. As recently as May of this year, the board of the AGA indicated by consensus that we would continue to oppose unregulated Internet gambling because we believe the technology does not currently exist to prevent underage gambling, to protect against pathological gambling, and to permit the strict regulation and law enforcement oversight required for integrity.

Thank you again for the opportunity to discuss our views on questions surrounding Internet gaming. I would be pleased to answer any questions you may have on this matter.

Frank J. Fahrenkopf, Jr.
President and CEO
American Gaming Association
Response to Internet Gaming Questions from Rep. Luis Gutierrez

1) **How could a successful regulatory scheme be set in place to protect from unregulated offshore sites?**
While our companies are not regulators, we do have experience as one of the most highly regulated industries in the country. I would suggest that you examine the regulatory structures in the states where our companies operate — Colorado, Illinois, Indiana, Iowa, Louisiana, Michigan, Mississippi, Missouri, Nevada, New Jersey and South Dakota — for guidance in developing a system that ensures the integrity of the games, polices against crime, minimizes the potential for money laundering and promotes the general welfare of the state. Another resource that might prove useful is the Gambling Regulation chapter in the National Gambling Impact Study Commission's final report, which included a "Best Practices Model for Casinos" developed by Michael Belletire, former chairman of the Illinois Gaming Board.

Even the best regulatory framework for commercial casinos, however, cannot overcome some of the challenges presented by offshore Internet gambling. The Nevada Gaming Commission is currently evaluating new technology that could be useful in the development of a regulatory framework for Internet gambling, including global positioning technology that could determine if a person placing a bet is in a locality that permits Internet gambling.

That said, the board of directors of the AGA is not convinced that the technology currently exists to provide adequate regulatory safeguards for American consumers.

2) **How do you believe that regulation of Internet Gambling would help prevent underage gambling and reduce the risk of developing gambling addictions?**
With commercial casinos nationwide, regulation provides certain safeguards that do not exist with offshore operators. For instance, all of our customers are required to be 21 years of age; severe penalties and fines are imposed against any operator who permits a minor to gamble, up to and including removal of a license. Regulation could require all operators involved in Internet gambling to use proven technology to prevent underage gambling with similar punishment for offenders.

One of the advantages of commercial casinos is that customers are physically present in our facilities, and some kind of intervention can occur with customers exhibiting signs of a gambling disorder. Depending on the specific situation, that intervention with customers could involve referral to educational brochures, a help line phone number or simply cutting them off. Being physically present also makes it easier for someone to ask for help. There are state "self-exclusion" programs as well that allow customers to ban themselves from a casino; names

and photos of those requesting this service are provided to security staff, and they are no longer permitted to enter the casino. While none of these programs is foolproof, they provide an added layer of safety that doesn't currently exist with Internet gambling. To provide those safeguards over the Internet, the Nevada Gaming Commission is currently examining several possible options, including establishing betting limits, time limits and a universal self-exclusion program, all of which might be considered if Congress were to look into regulating Internet gambling.

As I maintained in my statement before the subcommittee, I believe that any gambling operators with customers in the United States should be required to comply with the same federal and state laws followed by our companies.

Frank J. Fahrenkopf, Jr.
President and CEO
American Gaming Association
Response to Internet Gaming Questions from Rep. Sue Kelly

1) **Many believe that current law, including the Wire Act, makes Internet gambling illegal already. Do you agree with this interpretation of Federal law?**
I believe that the Wire Act as it is currently written prohibits sports betting but not casino gaming activity over the Internet.

2) **In your statement, you note that the official position of the AGA Board is in opposition to unregulated Internet gambling because the technology is not yet available to prevent underage gambling, protect against pathological gambling, and to permit the strict regulation and law enforcement oversight required for integrity. Can we interpret that to mean that the AGA is in favor of a Federal ban on Internet gambling at this time?**
Before the AGA takes a position on any bill, we would have to review it to ensure that it does not cause any unintended consequences or make something that is currently legal illegal. In principle, however, the AGA remains opposed to unregulated Internet gambling and would be supportive of appropriately drafted legislation.

3) **In your statement you express the AGA's major concern with the offshore Internet gambling sites that frustrate State gambling laws and regulations on gambling in their States. Obviously, the only reason offshore gambling is as easy as it is, is in part because of credit cards. Has the AGA ever talked to the credit card industry about this issue?**
The AGA met with a representative from the credit card industry to ascertain its position concerning the proposed Internet gambling prohibition legislation.

WRITTEN TESTIMONY OF WILLIAM S. SAUM
DIRECTOR OF AGENT, GAMBLING AND AMATEURISM ACTIVITIES
NATIONAL COLLEGIATE ATHLETIC ASSOCIATION
before the
HOUSE FINANCIAL SERVICES SUBCOMMITTEE ON
OVERSIGHT AND INVESTIGATIONS

July 12, 2001

Madame Chairwoman and members of the Subcommittee, thank you for the opportunity to testify on behalf of the National Collegiate Athletic Association (NCAA) and to share with you our concerns related to the growth and impact of sports gambling on the Internet. The NCAA is a membership organization consisting of nearly 1,000 universities and colleges and is devoted to the regulation and promotion of intercollegiate athletics for over 330,000 male and female student-athletes.

Though the growth of Internet gambling has seemingly sprouted overnight, this is not a new issue for the NCAA. For the past four years, we have worked with House and Senate sponsors in an effort to adopt legislation that would, in part, ensure that all sports gambling on the Internet is prohibited in this country. Why? The answer is quite simple. When people place wagers on college games there is always the potential that the integrity of the contest may be jeopardized and the welfare of student-athletes may be threatened. For example, many of you are aware of the recent point shaving scandals on the campuses of Northwestern University and Arizona State University. While these cases occurred before the rise of the Internet gambling industry, the impact of these sports gambling incidents must not be minimized. Millions and millions of dollars were wagered on the games. The result? Several of the student-athletes involved were indicted and sentenced to serve time in federal prisons. Coaches and teammates were betrayed and the two schools have seen their reputations tarnished. It is clear that sports gambling is not a victimless crime and that the potential for similar incidents to occur has increased now that sports bets can be placed on the Internet.

Perhaps the most frustrating aspect of Internet gambling is that while we all acknowledge the wondrous benefits of the Internet age, the Internet also has presented some significant challenges. Today, this new communications medium allows online gambling operators to circumvent existing U.S. laws aimed at prohibiting sports gambling. In 1961, Congress enacted the Interstate Wire Act that clearly prohibits interstate sports wagers transmitted over a wire communication facility. Yet Internet sports gambling continues to thrive in the U. S. and has grown largely unchecked. The challenge of effectively combating offshore Internet gambling operators is a different problem than the issue of telephone wagering with sports bookies that was confronting Congress four decades ago. This is why we believe that new federal legislation is needed to address the rapidly transforming world of gambling in cyberspace.

As you listen today to witnesses arguing the pros and cons of Internet gambling, please do not overlook the potentially harmful impact of this activity on young people. A growing consensus of research reveals that the rates of pathological and problem gambling among college students

are three times higher than the adult population. This fact surely did not go unnoticed when the National Gambling Impact Study Commission recommended a federal ban on Internet gambling in June 1999.

Just four years ago, when the NCAA became involved in the legislative effort to ban Internet gambling, there were four dozen Internet gambling sites. Now there are 1,400 unique Internet gambling Web sites. Today, college students are perhaps the most wired group in the U.S. They can surf the Web in their school library, in a computer lab or in the privacy of their dorm room. The emergence of Internet gambling enables students to wager behind closed doors, anonymously, and with the guarantee of absolute privacy. Furthermore, the ease and accessibility of Internet sports gambling creates the potential for student-athletes to place wagers over the Internet and then attempt to influence the outcome of the contest while participating on the court or playing field.

If left unchecked, the growth of Internet gambling could be fueled by college students. Today, college students are armed with the means to gamble on the Internet. A 2000 study by Nellie Mae indicates that 78 percent of college students have credit cards and 32 percent have four or more cards. The average credit card debt for undergraduates has risen nearly 50 percent in the past two years to $2,750.

In my position as the NCAA director of agent, gambling and amateurism activities, I have already seen how students are falling victim to the lure of Internet gambling. Offshore operators continue to implement aggressive marketing tactics. There are billboards promoting Internet gambling sites in cities across the country, student-athletes continue to complain about receiving unsolicited e-mails for sports gambling Web sites and there have been reports of individuals passing out flyers touting Internet gambling opportunities at fraternity houses. I have spoken with students who have lost thousands of dollars gambling on the Internet. In fact, last year at a congressional hearing we played a video tape account of a college student who, in just three months, lost $10,000 gambling on sports over the Internet. Prior to placing his first bet online, this student had never wagered on a sporting event. Please be assured that this student's experience is not unique. The NCAA has heard from others with similar stories and the media is widely reporting on this emerging problem among young people. Finally, our staff is beginning to process NCAA rules violation cases involving Internet sports gambling. There is no doubt that the Internet has made sports gambling more accessible than ever.

The popularity of Internet gambling is not being lost on corporate America. Despite a federal statute clearly prohibiting sports gambling over the Internet, many U.S. companies continue to profit from Internet gambling related activities. On July 6, the *New York Times* published an article that highlighted some of the companies who are reaping monetary rewards from their association with Internet gambling. Most disappointing was the cavalier response from two

popular Web sites that profit by posting Internet gambling advertisements. The article mentioned that both Google.com and Yahoo do not accept tobacco ads but do take advertising money from Internet gambling operators. A spokeswoman for Yahoo indicated that the company "probably" has the technology that would allow it to target the ads only in jurisdictions where they are legal but that Yahoo is not currently employing such technology. A Google.com vice president provided a more troubling response to the question of why they prohibit tobacco and alcohol ads but not Internet gambling advertisements. He indicated that "while smoking and drinking were legal and Internet gambling was illegal in many states, 'gambling is not in the same class for us.'" The purpose of citing these examples is not to single out these companies but rather to demonstrate the current environment that exists.

There is a real need for legislation to address the unique changes that technology can now offer gamblers in cyberspace. On the legislative front, the past four years have been marked by frustration. Those supporting efforts to adopt Internet gambling prohibition legislation have come very close to achieving their goal but, in the end, they have been thwarted by an aggressive and well-financed opposition. Unfortunately, with each passing year, the Internet gambling industry grows at an exponential rate. The NCAA supports legislative efforts that will ensure that gambling on sports over the Internet is prohibited. It is true that there are existing laws that already prohibit sports gambling in nearly every state. However, these laws were enacted before the rise of the Internet and do not adequately address the problem of sports gambling via this new communications medium.

Internet gambling, with its global reach, knows no geographic boundaries. Further, the Internet continues to evolve. No longer is everyone accessing the World Wide Web over standard phone lines. Wireless access is now the rage and these new developments enable people to place bets using their Palm Pilots and cell phones. Current law simply does not cover these wireless activities.

The real challenge is drafting legislation that will not only address the problems associated with Internet gambling but also provide an effective enforcement mechanism that will have an impact on these offshore gambling operations. The NCAA is pleased that the Subcommittee is concerned about Internet gambling. Last year, the House Banking and Financial Services Committee approved legislation that would have prohibited the use of credit cards in connection with illegal Internet gambling. As many of you know, some credit card issuers have already imposed voluntary restrictions prohibiting U.S. customers from using the their cards in any Internet gambling transaction. Unfortunately, the offshore operators are already a step ahead of the game. For example, on its Web site, onlinesportsbook.com alerts its customers that they may experience difficulties using their credit cards when placing wagers. Without referencing the legal issues behind these problems, the operator suggests that customers utilize the services of one of several online financial account intermediaries, including FirePay and Pay Pal. It is our understanding that the use of these financial intermediaries makes it difficult for any credit card company to determine whether a given transaction is being used for Internet gambling purposes. Further, it creates a much more tangled web for law enforcement to navigate through as they try to "follow the money."

Clearly, the crafting of legislation will not be easy but the NCAA urges this Subcommittee and Congress not to let this opportunity slip away. Thoughtful legislation can be successful in significantly curtailing the growth and popularity of Internet gambling in this country.

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August 14, 2001

Ms. Janice Zanardi
Committee on Banking and Finanical Services
2120 Rayburn House Office Building
Washington, D.C. 20515

Dear Ms. Zanardi:

Below are my responses to the questions raised by Congressman Gutierrez as a follow-up to the testimony I delivered on Internet gambling before the House Financial Services Subcommittee on Oversight and Investigations on July 12, 2001.

1. **What can credit card companies do to help reduce the problem of Internet gambling? What percentage of those debts do you estimate could be linked to Internet gambling?**

   We are still trying to learn more about the techniques related to following the trail of a credit card transaction used for purposes of placing an Internet gambling wager. As a result, it is difficult for me at this time to provide a strategy for credit card companies that will effectively address the problem. However, the NCAA has long been concerned about the blatant violations of U.S. law when it comes to placing bets on sports over the Internet. The 1961 Wire Act is clear that no sports bets can be placed interstate using wire communications facilities. My testimony referred to widespread abuses by offshore Internet operations that are effectively circumventing U.S. law through direct in-person solicitation, billboard advertising and by accepting bets on sport events from U.S. customers. Presently, the payment mechanism of choice for those participating in Internet gambling is credit cards. The offshore Internet gambling companies have already adjusted to the voluntary restrictions on credit card use in Internet gambling activities imposed by banks and other credit card issuers. Many Web sites are urging customers to use financial intermediaries like Pay Pal and Fire Pay. These services are being used to circumvent the restrictions imposed by credit card companies. In addressing this complicated issue, Congress must first enact legislation that updates or supplements the 1961 Wire Act and makes it clear that sports gambling interstate, using any communications technology, is prohibited. The enforcement mechanism used in this approach may include some focus on the use of credit cards. However, regardless of the enforcement approach adopted, law enforcement must make a commitment to enforce the new regulations and prevent companies, including credit card companies, from knowingly "aiding and abetting" in the violation of federal laws prohibiting Internet gambling. There are too many U.S. companies that are directly and indirectly profiting from an activity that in the area of sports gambling is already illegal in this country.

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I am not aware of any study that has linked Internet gambling to mounting credit card debt. Internet gambling is a relatively new form of gambling. However, given the widespread availability of credit cards and the ease of student access to the Internet, it would not be surprising that this is already a growing problem among college students. As I stated in my testimony, student credit card debt is rising on college campuses. Unfortunately, there is a dearth of gambling related research, especially as it pertains to young people. Our hope is that as the media, legislators and others shine the spotlight on this issue that it will spark more research in this area.

2. **Talk about people passing out flyers at fraternity houses, encouraging students to gamble on-line. What are colleges and universities currently doing, if you are aware, to address the problem? Are they doing enough?**

Internet gambling operators are aggressively marketing their services to college students. Again, the offshore operators realize that students have credit cards and are perhaps the most Internet savvy group in the U.S. I have heard from college administrators who have told stories of individuals conducting in-person solicitations at fraternity houses for Internet gambling Web sites. In addition, I have received a number of e-mails from student-athletes and athletics administrators who are being sent e-mails encouraging them to visit a gambling site. The pitch is familiar. Most sites are providing a sign-up bonus: a free $25 or $50 in your account after you register. It should also be noted that students are being subjected to advertising for Internet gambling in many other places. Ads are appearing on billboards, in newspapers, in sports publications and in many in-flight magazines.

The NCAA has an extensive sports gambling education program. We currently have four staff members devoted, in part, to educating our members on sports gambling issues. For example, last year, the NCAA arranged for a college student who incurred $10,000 in losses gambling on sports via the Internet to speak at three seminars for athletics administrators. In addition, the NCAA provides its members with numerous videos, seminars, reading materials and posters that address the dangers of gambling on sports.

Last year, the National Association of Student Personnel Administrators (NASPA) formed a gambling task force. The NCAA is represented on this task force. The task force agreed that before any action can be taken to address gambling on college campuses, there must be a clearer understanding of the extent of the problem. Presently, a pilot group of institutions is surveying students to determine gambling behavior on campus. The NCAA hopes that the results will provide a clearer picture of where future efforts must be directed.

Is there more that needs to be done? Absolutely. The NCAA will continue to do its share while educating and encouraging our members to do the same.

3. How should federal law be amended to address the problems raised by Internet gambling?

The NCAA has worked for the past four years with sponsors in the House and Senate to enact Internet gambling prohibition legislation. In the past, we have supported an approach that would not amend the existing Wire Act but would, instead, create a new section, 1085, that would prohibit Internet gambling. The enforcement mechanism was modeled after the Internet service provider blocking provisions contained in the Digital Millennium Copyright Act. We believe this enforcement mechanism would be effective and is currently achievable without placing significant burdens on Internet service providers. However, since the end of the 106th Congress, an enforcement mechanism focusing on credit card use has been widely discussed. While we are still examining this approach, if law enforcement and the appropriate federal agencies believe this would be an equally effective approach in prohibiting illegal Internet gambling activity, we would likely be supportive.

The NCAA believes that it is critical for Congress to act now and adopt legislation that addresses the problem of Internet gambling. Experts like Sebastian Sinclair have been signaling that the Internet gambling industry is on the verge of a major consolidation. As large, multinational corporations (many with U.S. land-based interests) begin to enter the Internet gambling industry, these companies are far more likely to abide by a clear U.S. prohibition than the rogue, small companies that currently dominate the scene today. The NCAA is supportive of new legislation that will send a clear message that it is illegal for businesses to solicit or accept sports bets in the U.S. over any communications medium. Already some offshore gambling companies are blocking wagers coming from the U.S. A new law would clearly have a positive impact in driving the rest of the industry to do the same. While it is likely that the Internet gambling industry will continue to expand internationally, the passage of federal legislation in Congress will, at a minimum, go a long way to ensuring that it does not grow with the involvement of the U.S.

If you should have any further questions, please do not hesitate to contact me at 317/917-6222.

Sincerely,

William S. Saum

William S. Saum
Director of Agent, Gambling
and Amateurism Activities

WSS:scp

cc: The Honorable Luis Gutierrez

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August 14, 2001

Ms. Janice Zanardi
Committee on Banking and Financial Services
2120 Rayburn House Office Building
Washington, D.C. 20515

Dear Ms. Zanardi:

Below are my responses to the questions raised by Congresswoman Kelly as a follow-up to the testimony I delivered on Internet gambling before the House Financial Services Subcommittee on Oversight and Investigations on July 12, 2001.

1. **Has the NCAA ever held discussions with the credit card companies about their role in facilitating on-line gambling and in making easy credit available to college kids?**

   The NCAA has not met with credit card companies to discuss the issue of on-line gambling. Presently, we are in the process of developing a dialogue with federal law enforcement and Treasury Department officials to explore the use of credit cards in illegal Internet gambling transactions. After we get a better understanding of the complexities in monitoring credit card transactions and what would be the most effective methods for limiting their use in Internet gambling transactions, we will be in a more informed position to discuss this issue with credit companies.

2. **Mr. Sinclair argued in his testimony that it will be impossible, as a practical matter, to ban Internet gambling, just as prohibition failed to stop the consumption of alcohol in this country. Do you agree? Does law enforcement have the necessary technological ability to enforce such laws?**

   The NCAA does not agree with Mr. Sinclair's conclusion as it applies to Internet gambling in the U.S. For the past four years, the NCAA has worked with sponsors in the House and Senate to enact Internet gambling prohibition legislation. Much of this time was spent examining effective enforcement options. The enforcement mechanism contained in previous legislation was modeled after the Internet service provider blocking provisions contained in the Digital Millennium Copyright Act. We believe this enforcement mechanism would be effective and is currently achievable without placing significant burdens on Internet service providers. It is our understanding that most Internet service providers are already engaged in blocking activities. In addition, this approach received the support of the National Association of Attorneys General.

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However, since the end of the 106th Congress, an enforcement mechanism focusing on credit card use has been widely discussed. While we are still examining this approach, if law enforcement and the appropriate federal agencies believe this would be an equally effective approach in prohibiting illegal Internet gambling activity, we would likely be supportive.

More importantly, as it relates to the United States, Mr. Sinclair has indirectly provided an argument for why federal legislation would have a significant impact in greatly curtailing Internet gambling activity in this country. Mr. Sinclair has long been arguing that the Internet gambling industry is on the verge of a major consolidation. As large, multinational corporations (many with U.S. land-based interests) begin to enter the Internet gambling industry, these companies are far more likely to abide by a clear U.S. prohibition than the rogue, small companies that currently dominate the scene today. The NCAA is supportive of new legislation that will send a clear message that it is illegal for businesses to solicit or accept sports bets in the U.S. over any communications medium. Already some offshore gambling companies are blocking wagers coming from the U.S. A new law would clearly have a positive impact in driving the rest of this rapidly changing industry to do the same. While it is likely that the Internet gambling industry will continue to expand internationally, the passage of federal legislation in Congress will, at a minimum, go a long way to ensuring that it does not grow with the involvement of the U.S.

3. **What role should personal responsibility play in preventing irresponsible gambling among college students? Isn't it a bit much to emphasize the passage of new laws to the exclusion of other efforts to prevent problem gambling? What other programs does the NCAA offer to help students with gambling problems?**

The NCAA believes that new federal legislation, aggressive enforcement efforts by law enforcement and strong education awareness programs are all critical components to addressing Internet sports gambling. The NCAA has an extensive sports gambling education program. We currently have four staff members devoted, in part, to educating our members on sports gambling issues. For example, last year, the NCAA arranged for a college student who incurred $10,000 in losses gambling on sports via the Internet to speak at three seminars for athletics administrators. In addition, we utilize a multitude of tools to reach student-athletes and coaches with our message about sports gambling. These efforts include videos, seminars, reading materials and posters that address the dangers of gambling on sports. An example of our concern regarding sports gambling is illustrated in our annual locker room discussions with members of the Final Four men's and women's basketball teams, the Frozen Four teams, and the finalists of the College World Series.

In addition to delivering our message to student-athletes, we also have developed relationships with and made presentations to various law enforcement groups, including the

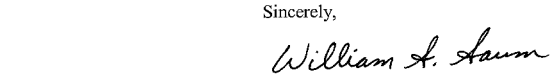
FBI and the United States Attorney General's Advisory Group, the American Council on Education's secretariat, campus security officers and coaches associations.

Also, this issue has begun to resonate with the larger higher-education community. The National Association of Student Personnel Administrators (NASPA) last year formed a gambling task force. The NCAA is represented on this task force. The task force agreed that before any action is taken to address gambling on college campuses, there must be a clearer understanding of the extent of the problem. Currently, a pilot group of institutions is surveying students to determine gambling behavior on campuses. The NCAA hopes that the results will provide a clearer picture of where future efforts must be directed.

Is there more that needs to be done? Absolutely. The NCAA will continue to do its share while educating and encouraging our members to do the same.

If you should need any additional information, please do not hesitate to contact me at 317/917-6222.

Sincerely,



William S. Saum
Director of Agent, Gambling
and Amateurism Activities

WSS:scp

cc: The Honorable Sue Kelly

WRITTEN STATEMENT

OF

MARK MACCARTHY

SENIOR VICE PRESIDENT

PUBLIC POLICY

VISA U.S.A. INC.

Before the

SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATIONS

of the

COMMITTEE ON FINANCIAL SERVICES

U.S. HOUSE OF REPRESENTATIVES

July 12, 2001

Chairwoman Kelly, Ranking Minority Member Gutierrez, and Members of the Subcommittee, my name is Mark MacCarthy, and I am Senior Vice President for Public Policy for Visa U.S.A. Inc. Thank you for the invitation to participate in this hearing on Internet gambling.

The Visa Payment System is a membership organization comprised of 21,000 financial institutions licensed to use the Visa service marks. It is the largest consumer payment system in the world. Over 1 billion Visa-branded cards are accepted at over 20 million locations worldwide. Consumers use their Visa cards to buy over $1.8 trillion in goods and services around the world. Visa U.S.A., which is part of the Visa Payment System, is comprised of 14,000 U.S. financial institutions. U.S. customers carry about 350 million Visa-branded cards and use them to buy over $900 billion worth of goods and services annually.

In addition, it is important to note that Visa credit cards and debit cards are general purpose access devices that can be used at millions of merchant locations around the world -- including more than 4.3 million merchant outlets in the United States alone. Card issuers in other payment systems also issue millions of cards, and financial institutions open tens of millions of checking accounts, and these cards and accounts also can be used in transactions around the world.

VISA INITIATIVES

Visa has taken several steps to address Internet gambling. Our general policy is that Visa cards should be used only in connection with legal transactions. Visa card issuers are required by Visa to advise cardholders of this fact and explain that Internet gambling may be illegal in some jurisdictions and that their cards should be used only for lawful transactions. On the Visa Web site, we post the same warning:

> **Get the facts on Internet gambling.**
> Internet gambling may be illegal in your jurisdiction. Since Visa cards may only be used for legal transactions, you should confirm whether your jurisdiction allows gambling before paying with your Visa card. Display of a payment card logo by an online merchant does not mean that Internet gambling transactions are lawful in all jurisdictions in which cardholders are located.

While Visa card issuers are required to advise their cardholders that Internet gambling may be illegal in certain jurisdictions and that Visa cards should only be used for lawful transactions, we do not otherwise impose restrictions on the use of Visa cards for legal purposes. However, Visa U.S.A. has no interest in promoting Internet gambling. Internet gambling is a negligible part of the total transaction volume that flows through the Visa system; and Internet gambling transactions pose legal and operational risks for our members, including bad debts, enforcement problems and legal expenses.

Visa also understands that Internet gambling sites are illegal in most states, and we work cooperatively with law enforcement agencies in their efforts to put these operations out of business. When enforcement agencies come to us for information about a particular domestic site that they believe is involved in Internet gambling, we cooperate with them fully. When we receive independent information that a domestic site is accepting Visa cards for Internet gambling purposes, we inform law enforcement agencies.

Visa recognizes that Internet gambling can raise important social issues, especially regarding the access that the Internet can provide for problem and underage gamblers. Internet gambling also can create financial risks and customer service problems for our member financial institutions. For both these reasons, Visa has taken steps to enable Visa members to employ systematic declines for potentially illegal Internet gambling transactions. Some members also have established their own internal procedures to block gambling transactions, whether legal or illegal.

However, the sheer volume of transactions that flow through the Visa system requires us to rely on a merchant coding system to ascertain the nature of particular transactions. The Visa system now operates at a pace of 35.5 billion transactions per year. Visa currently processes an average of 2,500 messages per second, and has a peak capacity of 4,000 messages per

second. In an attempt to identify Internet gaming transactions without impairing the operation of the Visa system, Visa requires Internet gaming merchants that accept Visa payment cards to use a combination of the "gaming" merchant category code and the electronic commerce indicator code for all gaming transactions. These two codes are transmitted through the Visa network as part of the authorization message. The combination of these two codes informs the card issuer that the transaction is likely to be an Internet gambling transaction, and thereby enables the issuer to deny authorization for such transactions to protect the interests of both the card issuer and its cardholders. Many issuers have taken advantage of this capability and other tools they have devised to deny authorization to any transaction coded as an Internet gambling transaction.

Any such coding system has limitations, however. First, it depends on the merchant to accurately code a transaction. Visa merchants are required to properly code transactions, and there are penalties for failure to do so. But there are obvious incentives for some Internet gambling merchants to try to hide from Visa and its members. They know perfectly well that coding the transactions properly could result in a denial of authorization, and the incentives will only increase as more Visa issuers decline authorizations.

Second, the coding only informs the card issuers that the transaction is likely to be an Internet gambling transaction; it cannot tell the issuer whether this particular transaction is illegal or not. For example, a cardholder may be using his or her credit card to purchase non-gambling items on an online casino Web site and those purchases may be identified as Internet gambling transactions under the codes described above. In addition, Internet gambling is legal in many foreign countries and for certain types of gambling. U.S. cardholders may visit these foreign countries and while there, use their credit cards to pay for online gambling transactions in a fully legal manner. Thus, not all transactions that would fall under the codes described above are illegal Internet gambling transactions.

In addition, the coding system applies only when an online gambler uses a Visa card to purchase goods and services from an online gambling merchant. But online gamblers often use the various electronic cash and account funding systems that create pools of electronically available funds which can be used for auctions, online purchases or possible Internet gambling. Thus, a cardholder could use his or her credit card to purchase e-cash on a Web site that does not itself offer gambling, but allows that e-cash to be used on another Web site that does offer gambling. The coding system described above would not capture these transactions as Internet

gambling transactions. It is our belief that these alternative forms of payment will become the payment system of choice for Internet gambling, in part to avoid the coding and blocking systems that Visa and the other traditional payment systems have established.

Even though the coding system is not perfect, it does give issuers an increased ability to identify potential Internet gambling transactions and the flexibility to deny authorization for potential Internet gambling transactions to protect the interests of both the card issuers and their cardholders.

LEGAL AND LEGISLATIVE ISSUES

While Visa has a general policy of prohibiting the use of its cards for illegal purposes, it is impossible for us or for any financial institution to determine quickly and efficiently whether a particular Internet gambling transaction is illegal. For example, as indicated above, Internet gambling is legal in many foreign countries. Internet gambling also may become legal in some states (like Nevada), or in some parts of states (like Indian reservations), or throughout states for certain types of gambling (like a charitable lottery). A complex case-by-case examination would be required with respect to each Internet gambling transaction to determine whether a particular Internet gambling transaction is illegal.

Part of the problem is simply ascertaining where a cardholder is originating the transaction. The same card could be used from a computer in the cardholder's home, where for the sake of argument let us assume that Internet gambling is illegal, or it could be used from a computer in a foreign country, or in international waters, where Internet gambling is clearly legal. It is impossible for a payment system to determine, from the information available to it, which of these circumstances is true in any particular case. After the fact it might be possible to detect the physical location of the merchant, but a payment system is not able to determine the physical location of the cardholder at the time of the transaction.

More fundamentally, however, the legal status of placing a bet on the Internet is not clear. When the gambler is located in a foreign jurisdiction which allows Internet gambling, does the law of that jurisdiction apply? The law is not clear at this point. It is clear that the operation of an Internet gambling site in the United States is illegal under most state laws, but we understand that it is still uncertain whether an individual in the privacy of his own home who travels via the Internet to an online gambling site in Antigua is violating the law.

Going forward, it is our view that the responsibility for illegal acts should be placed squarely on the shoulders of the illegal actors

themselves -- the gamblers and the casinos who are engaging in illegal gambling activities. Payment systems operators, like Visa, are not in the gambling business. They assist participating financial institutions, merchants and cardholders throughout the world to promptly and efficiently engage in tens of billions of transactions every year. As indicated above, the Visa system alone currently is running at a pace of 35.5 billion transactions per year. The overwhelming majority of these transactions are lawful transactions in every respect, and are fundamental to the successful operation of the U.S. marketplace and those of many other countries as well.

Policymakers may be looking for a simple and effective way to control Internet gambling. But controlling Internet gambling is legally and operationally complicated for all payment systems, including Visa. Making payment systems responsible for policing Internet gambling simply is not a quick fix toward solving a complex social problem. Moreover, legislation authorizing the Justice Department or regulators to require Visa to cut all Internet gambling merchants off from the payment system would be a first. We are aware of no other case where law enforcement agencies have the authority to force private payment systems to become their deputies in order to exclude merchants -- who are engaged in a legal business -- from the payment system. Moreover, it is not necessary. Visa has a proud and long

history of working cooperatively with law enforcement agencies to aid their prosecution of a wide variety of criminal activities, from fraud to money laundering.

Finally, it is hard to see how Congress can address the role of payment systems in Internet gambling without clarifying the underlying legal landscape. To merely state that payment systems should block all Internet gambling transactions means that if we are successful, we will be preventing people from using their payment cards for perfectly lawful activities. To say that we should block all illegal Internet gambling transactions, without clarifying which ones are illegal, would put us in the impossible position of interpreting laws in myriad jurisdictions.

Even a law that makes all Internet gambling illegal would be hard for us to enforce. As mentioned before, a payment system depends entirely on coding by the merchants. If policymakers declare Internet gambling illegal, unscrupulous merchants will simply stop coding their transactions as Internet gambling, and payment systems will be unable to detect them.

Conversely, a more complex law that allows for multiple exceptions from a ban on Internet gambling, that allows such gambling to take place on an intrastate basis or that permits certain classes of gambling -- charitable lotteries or pari-mutuel betting, for example -- would be impossible for any

payment system to enforce. Even the most sophisticated coding system simply could not reflect these variations.

We appreciate the opportunity to testify and would be pleased to answer any questions.

Responses to Questions from Congressman Luis Gutierrez

(1) Mr. MacCarthy, you heard Mr. Saum's testimony stating that 50% of college students have an average debt of as much as $2,750. What is Visa doing to address this problem?

The General Accounting Office's recent report on college marketing of credit cards confirms that students can benefit from many advantages when they use credit cards responsibly. These advantages include: credit cards are secure, are helpful in case of emergencies like broken down cars and medical expenses, can be used to purchase school supplies, are safer than cash and are helpful to students in establishing a credit history.

In addition, experience shows that the credit performance of young adults is similar to that of the population at large -- the majority handle credit responsibly and only a small percentage experience financial difficulty. For instance, a 1998 survey conducted jointly by The Education Resources Institution and the Institute for Higher Education Policy showed that 59% of college students reported paying their balances in full each month and, of the 41% who carried a balance, 81% paid more than the minimum amount due. *(TERI/IHEP Credit Card Survey, March/April 1998.)* Likewise, a 2000 survey conducted by the Student Monitor showed that 58% of college students reported paying their balances in full each month. (*Student Monitor Survey, Spring 2000.*)

The creditworthiness that is demonstrated by young adults is not surprising, considering the steps that the credit card industry has taken to provide young adults with better tools to help them make informed, responsible money management decisions. Visa has long worked with parents and schools to teach young people practical money skills before they leave home and when they are away at school. For example, most recently, Visa has partnered with teachers to provide free learning tools through our online resource center: www.practicalmoneyskills.com. In particular, this Web site contains a teacher-tested comprehensive online resource with online calculators, downloadable financial education curriculum in both English and Spanish and free games. Through this online curriculum, Visa is working with financial experts and important groups like the Jump$tart Coalition for Personal Financial Literacy and the National Consumers League to give parents and teachers resources to help students learn the basics, like saving, making a budget and sticking to it. Visa is supportive of these financial education efforts, because we believe that financial education is the best way to promote fiscal responsibility.

(2) How much have Visa's Internet gambling-related revenues approximately increased in the last 2 years?

Notwithstanding the introduction of e-commerce and gaming codes among the transaction codes that are to be used by merchants participating in the Visa system, it still is not possible for Visa to identify accurately all Internet gambling transactions, let alone estimate the transaction processing fees that result from such transactions. Nonetheless, Internet gambling is, at best, a negligible part of Visa's total system revenue. The entire Internet gambling industry's volume has been estimated by some at $1.5 billion. Visa would only process a portion of those payments. Last year, for all merchants worldwide, Visa processed more than $1.8 trillion in total payments. As a result, it is likely that any transaction processing fees received by Visa from processing Internet gambling transactions are insignificant, perhaps pennies per thousand dollars of volume.

Responses to Questions from Congresswoman Sue Kelly

(1) Many believe that current law, including the Wire Act, makes Internet gambling illegal already. However, you assert on page 7 of your written testimony "that it is still uncertain whether an individual in the privacy of his own home who travels via the Internet to an online gambling site in Antigua is violating the law." What is your interpretation of Federal law? Are you saying that it might indeed be legal for Americans to participate in Internet gambling at offshore sites?

The fact that there are a number of bills pending in Congress and in state legislatures to make all or some forms of Internet gambling illegal suggests that its current legal status is unclear. Last year the U.S. Department of Justice testified before Congress asking that the Federal Wire Act be amended so that it clearly applies to all betting or wagering and includes the transmission of bets or wages on any communication facility. The Department added that this amendment "would eliminate any doubt about whether section 1084 (of the Wire Act) only applies to bets or wagers on sporting events and contests. It would also ensure that future technologies that are not wire-based communication facilities are covered..." After that testimony, the United States District Court for the Eastern District of Louisiana ruled that the Wire Act prohibited sports gambling on the Internet but that the Act did not ban casino gambling on the Internet.

Internet gambling transactions between a merchant in one jurisdiction and a customer in another raise choice of law and choice of jurisdiction issues that have not been fully resolved. In one case, a French court extended its jurisdiction to Yahoo, Inc., a U.S. merchant, and ordered it to block transactions between French citizens and U.S. entities selling Nazi paraphernalia. Yahoo is currently appealing the French court's order before the United States District Court for the Northern District of California San Jose Division. A coalition of US companies, including the U.S. Chamber of Commerce, the U.S. Council for International Business, and the Information Technology Association of America, has filed an Amici Curiae brief with the court objecting to the idea that courts in France can assert jurisdiction over a U.S. company and mandate that the company block French citizens' access to material on the Yahoo website.

The Cohen case in New York raises jurisdictional issues similar to those raised in the Yahoo case. In this case, a defendant accused of illegal Internet gambling under the Federal Wire Act asserted that his activity was legal because his site was in Antigua and Internet gambling is legal in Antigua. The trial court ruled against him. He appealed to the New York 2nd Circuit Court of Appeals, and, at the time of my testimony, his appeal was pending. Since then, on August 1, 2001, he lost his appeal. He is considering his options, which include asking for a rehearing, asking for an "en banc" hearing before the full appeals court, or appealing to the U.S. Supreme Court.

(2) You note that there are "penalties" for failing to code a transaction properly. What kinds of penalties are we talking about? Has Visa ever withdrawn authorization for use of its card from an Internet gambling establishment that

miscodes gambling transactions in order to deceive US financial institutions into paying gambling debts?

Visa does not have direct contracts with either cardholders or merchants. It is an association of some 21,000 member banks worldwide that compete for contracts with the cardholders (the Issuers) and the merchants (the Acquirers). Visa sets standards and rules for Issuers and Acquirers, as well as penalties for failure to follow those standards and rules. The member banks, in turn, may then impose these fines on merchants. Visa's penalties for miscoding transactions can run to tens of thousands of dollars, based on the number and severity of violations. Visa has not yet withdrawn authorization for merchant acceptance of its card because when it investigates a complaint regarding improperly coded gambling transactions, the establishments contacted have complied with coding requirements. However, it is fully prepared to withdraw authorization if necessary.

(3) Let me ask a questing about making Internet gambling debts legally "unrecoverable." I understand that the National Gambling Impact Study Commission recommended that such debts be made unrecoverable by law. In addition, there was a 1998 court case involving a California resident who had lost more than $70,000 through Internet gambling, but who, when sued by her bank for nonpayment of credit card debts, countersued claiming that credit card companies were engaged in illegal profit taking from Internet gambling. Although that suit was settled out of court, isn't Visa facing a precarious situation if debt acquired through illegal offshore Internet gambling activities were to be held "unrecoverable" by a court?

A gambling debt is the amount owed by a bettor to the casino or other gambling establishment as a consequence of placing a bet and losing. Statutes denying enforceability to gambling debts are directed at those involved in gambling activity. Visa member banks are not engaged in the gambling business. They have lent money to a cardholder, which the cardholder used as he or she chose. The cardholder owes the debt to the issuer not to the merchant or to any other party. In the California case you mention, Visa and its member banks made no acknowledgement that amounts owed were gambling debts. In fact, Visa and its member banks who were party to that settlement agreement made no payments or forgave any Visa card debt to any party in that suit.

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TESTIMONY OF MS. SUE SCHNEIDER

CHAIRMAN, INTERACTIVE GAMING COUNCIL

before the

SUBCOMMITTEE ON OVERSIGHT AND INVESTIGATION

of the

HOUSE COMMITTEE ON FINANCIAL SERVICES

"INTERNET GAMBLING: GOOD GAMBLING OR BAD BET?"

July 12, 2001

Madam Chairwoman and Members of the Committee, my name is Sue Schneider and I've served as Chairman of the Interactive Gaming Council since its formation in 1996. I'd like to applaud you for holding this hearing to educate yourselves on the public policy issues regarding Internet gambling and particularly for inviting the affected industry to present comments. It's a complex topic that requires open debate.

The Interactive Gaming Council (IGC) is a not-for-profit trade association with over 100 member companies from around the world. These companies are operators, software suppliers, e-commerce providers or ancillary services providers like my own company, which offers information services. The mission of the organization is to provide a forum for what we consider to be the legitimate participants in the industry; to provide uniform standards for those participants, and to provide a unified voice to advocate for the interests of our members and the consumers who enjoy their services.

The IGC has noted the concerns voiced by many in Congress regarding consumer protections with respect to on-line gaming. The IGC shares these concerns and has therefore created a Code of Conduct (Appendix A), Responsible Gaming Guidelines (Appendix B) and most recently, a Seal of Approval program (Appendix C). We believe that neither governments nor consumers will long tolerate an industry which does not extend adequate protections to its consumers. Thus, our members feel that we must work with those governments globally in an effort to offer solid regulatory environments.

Having discussed briefly what we are, I suppose I should devote a little attention to what we are *not*. IGC members are *not* the sort of "fly by night" operators who set up an operation, place a few banner ads, accept a few million in wagers, fail to pay out winnings, and shut down two weeks later – indeed our organization is meant to be the antidote to that. We are *not* advocates of a sort of "wild west" approach to Internet gaming where the only governing principle is that of *caveat emptor*. Finally, we are *not* unaware of, or insensitive to the issues of underage or problem gaming. We believe that regulation – first industry self-regulation, and ultimately rational government regulation, are the solutions to these problems.

There are currently 54 governments which offer some form of interactive gambling regulatory infrastructure (Appendix D) and the number is growing. Countries such as Great Britain and South Africa are now exploring regulatory structures. One of our initiatives is to work with the international body of gambling regulators so that baseline standards are developed that address concerns such as underage gambling, compulsive gambling, game testing, money laundering and others. I'd be happy to give you more details on these frameworks in the question period.

You're likely aware that some states in the US are beginning to explore the development of regulatory structures to govern this activity. Most notable is Nevada, which last month passed enabling legislation authorizing its Gaming Commission to explore the situation. Additionally, some state lotteries have expressed interest in providing tickets online, and in the closing days of

the 106th Congress, Congress extended protection for the horse-racing industry to accept online bets.

This fledgling segment of the gambling industry is one of the few profitable business sectors on the Internet and it is growing. Estimates are that it is currently a US$3.1 billion industry this year, expected to grow to US$6.3 billion in 2003. (Appendix E) Globally, approximately 325 operating companies and governments offer their products through these new electronic delivery systems on 1,400 websites. These include sportsbetting, casino games, lotteries, racing, bingo and the newest entry, person to person betting. The nature of the business is shifting with an increasing number of terrestrial gambling operators now bringing their products online as an adjunct to their land-based business.

Somewhat surprisingly, 50%-90% of the market demand for these services is coming from the US. This is expected to drop as a percentage of the whole in the future as Internet penetration grows in other parts of the world, particularly those areas where gambling doesn't have the stigma which it has here. (Appendix F)

There are clear public policy challenges in this discussion. Among these are:

- State vs. federal oversight
- The location of where the gambling transaction occurs (important for tax collection)
- Multijurisdictional harmonization of regulations

This Committee's specific concern is the role of financial transactions in this industry. Clearly, these are the lifeblood and without them, deposits can't be made nor players paid. I would hope that you refrain from putting financial institutions and processors in the role of policemen because of the precedent it will send out to the world regarding the US attitude toward e-commerce. If financial instruments are treated as the regulatory chokepoint for e-commerce, it seems quite likely that governments at every level and around the world will seek to have financial institutions enforcing a patchwork of laws and regulations that could make e-commerce completely unmanageable. Such a move will only speed up the evolution of truly anonymous e-cash services as an alternative for those players who want to play, something that is not desirable by governments or responsible participants in the industry.

You've also asked us to address the issue of money laundering. This is a critical issue internationally, especially since many of the licensing jurisdictions are currently "offshore" in Europe, the South Pacific and the Caribbean. For consumers, trying to launder any quantity of funds via an online gaming site is fairly cumbersome and raises red flags with operators. Of more concern is a pseudo-operator who may be laundering money. Again, with solid and consistent international regulatory requirements such as background checks, this can be controlled.

Madam Chairman, I would ask that you keep two pieces of history in mind as you explore this issue. One is the Volstead Act, the 1920s alcohol prohibition, in which the federal government attempted to curb a highly popular activity among the American people. That act set out to protect America against the ravages of alcoholism. However, then as now, the vast majority of people who

drank were not problem drinkers. Its primary impact was to create an underworld crime organization which has lasted for years. It failed further in that it prevented responsible drinkers from enjoying the pleasures of a social drink, but did almost nothing to keep alcohol from the problem drinkers it set out to help. I would suggest that attempts to prohibit Internet gaming would see similar results – it would frustrate those who currently wager harmlessly online, and it might set precedents which would do much harm to all of e-commerce, but it will do little to help those it seeks to help.

The other historical example is that of Las Vegas. What began as an unregulated oasis in the desert has slowly evolved into a highly regulated and successful tourism spot with tax revenues which support an entire state. Government and industry work together to allow people access to an activity they enjoy, and at the same time, to minimize the harmful side effects of that activity. The IGC and its members are eager to work with policymakers at any level of all governments to see Internet gaming follow this path. This committee and this Congress must choose which of these historical precedents to follow. The IGC and its members would urge you to choose the latter.

Once again, I thank you for the opportunity to testify, and look forward to the questioning period.

APPENDIX A

CODE OF CONDUCT

1. **Regulatory Compliance:** All IGC members will abide by the law and regulations of the jurisdiction where they propose to do business. Any IGC member issued a bona fide gaming license from a sovereign jurisdiction shall provide evidence of that license and will be presumed to be operating under the authority and within the scope of that license. IGC members shall use best efforts to obtain any binding legislative or judicial determinations which prohibit or limit operation in another jurisdiction and shall abide by those limitations to the greatest extent technically feasible.

2. **Accountability:** To enhance customer confidence in gaming system integrity, IGC members making their service available in a jurisdiction voluntarily agree to make their systems, algorithms and practices available for inspection and review by any legitimate gaming commission or governmental authority or to any independent testing authority recognized by the IGC, in accordance with generally accepted methods for protecting proprietary information.

3. **Consumer Privacy and Data Protection:** IGC members will design and operate their services to afford customers privacy and confidentiality and will post their confidentiality practices and procedures. Each IGC member will institute controls to detect and eliminate fraud and to protect data and the system from internal and external breaches.

4. **Truth in Advertising:** IGC members shall be truthful in all promotions and publish only accurate information about their operations. Gaming and Wagering Operator Member rules, registration procedures and payout percentages will be made available to the public.

5. **Dispute Resolution and Audit Trails:** In order to provide prompt and efficient dispute resolution each IGC member will retain detailed transaction records which will be archived, accessible and auditable by any legitimate gaming commission or government authority.

6. **Limiting Access by Minors:** IGC members will institute adequate controls to prohibit minors from accessing their gaming systems. The controls will require customers to affirm that they are of lawful age in their jurisdiction, and the IGC member shall institute reasonable measures to corroborate this information.

7. **Controlling Compulsive Gambling:** IGC members will implement adequate procedures to identify and curtail compulsive gambling. The procedures instituted shall include posted loss limits, and provision of referral and direct access to help and counseling organizations.

8. **Banking and Transaction Processing.** IGC members will conduct their banking and financial affairs in accordance with generally accepted standards of internationally recognized banking institutions. Members will follow and adhere to all jurisdictional laws pertaining to transaction reporting.

9. **Prize Payouts:** Interactive Gaming and Wagering Operators will ensure that there is adequate financing available to pay all current obligations and that working capital is adequate to finance ongoing operations. IGC members will pay winnings and account balances promptly on demand.

10. **Corporate Citizenship:** IGC members will endeavor to design and implement their services in order that they preserve and protect environmental resources, avoid depiction of violence and so that the services are user friendly and generally accessible to the handicapped. IGC members will endeavor to support public service initiatives in harmony with the jurisdictions in which they provide their services.

For further information please do not hesitate to contact Rick Smith or Keith Furlong by email at executive.director@igcouncil.org or keith.furlong@igcouncil.org respectively.

APPENDIX B

RESPONSIBLE GAMING GUIDELINES

Interactive Gaming Council Responsible Gaming Issues are:

- The Interactive Gaming Council (IGC) will develop, advertise, implement and evaluate industry-wide Policies and Procedures for Responsible Internet Gaming.
- IGC members shall make every effort to identify possible compulsive and problem gamblers and shall further make a reasonable effort to address the consumer's potential problem.
- To facilitate an appropriate action, IGC members shall voluntarily seek training from professionals whose area of expertise addresses prevention, identification, intervention and referral of compulsive/problem gamblers to assistance programs. The Responsible Gaming Committee will provide assistance in identifying these professionals and programs and convey this information to IGC members.
- To show support of providing help to compulsive/problem gamblers, IGC members shall promote "the 20 Questions of Gamblers Anonymous" and/or other compulsive/problem gambling screening tools for their customers.
- IGC members shall make available information and links to guide compulsive/problem gamblers to supportive gambling helplines and information sites. The Responsible Gaming Committee will provide various methods of displaying these links for use on member websites.
- IGC members shall support and adhere to betting limits in an attempt to identify and limit compulsive or problem gamblers. This will include: oversight of the use of multiple credit card accounts by customers; the establishment of personal betting limits; and the monitoring of customers' account access experience. Such oversight and monitoring may provide for a 24-hour "cooling off period" when betting limits are reached, or more than three (3) account access attempts are made within a twenty-four hour period.
- The Responsible Gaming Committee will work with IGC members in establishing and refining techniques to discourage problem gaming. IGC members shall make every effort to implement security measures to prevent access to gaming accounts by underage Internet users, and shall post a voluntary Age Restriction Notice.
- When made available, IGC member sites will utilize rating standards that provide for content registration (for example, PICS rating standards), and blocking software to parents, in an effort to curtail access by underage Internet users. The Responsible Gaming Committee will provide assistance in identifying technologies in this area, and how they can best be used.
- When provided and approved by the IGC, member sites agree to adopt self-regulatory controls, and/or agree to adhere to the regulations established by the jurisdiction under which the member's license was granted.
- IGC members are encouraged to make donations to organizations who provide assistance, programs and services to compulsive/problem gamblers, and to report such donations to the Responsible Gaming Committee for press and/or public relation releases.
- IGC members shall make every effort to provide self-restriction controls in their customer databases for those compulsive/problem gamblers who submit such self-imposed restrictions to a gaming site in writing.
- IGC members agree not to extend credit to gambling patrons.

APPENDIX C

SEAL OF APPROVAL

The goal of the IGC's Seal of Approval (SOA) program for the interactive gaming industry is to provide a foundation for greater public confidence, respectability and credibility.

By participating in the SOA a participant displays a commitment to business integrity and to complying with a set of established guidelines and IGC Code of Conduct.

SOA participants display a seal that indicates to consumers the site's willingness to adhere to a new, higher level of compliance as a supplement to existing government regulatory regimes. To be a successful SOA applicant a member will have to satisfy criteria pertaining to the applicant's good standing as an IGC member for a qualifying period of time as well as being subjected to a more comprehensive due diligence check.

A successful SOA applicant agrees to accept and adhere to the SOA program rules and guidelines and will be provided with a recognizable logo to display on their gaming site. The seal represents a participant's agreement to adhere to a higher set of standards toward an honest and fair gaming environment. An important component is a formalized dispute resolution process for dissatisfied players.

The Internet gaming industry is dynamic, exciting, and in many cases responsible. The IGC's Seal of Approval program will allow operators to show support for on-line gaming environments that are fair and honest.

One important issue that should be addressed is the issue of government regulation. The Seal of Approval is by no means designed to be a replacement for strict government regulation. In fact, the IGC has been actively advocating strict licensing and regulation by governments. It is the opinion of the IGC and its members that effective government regulation is the only way to move the Internet gaming industry to the next level of legitimacy. Further, the IGC believes that since access to Internet gaming sites cannot be effectively prohibited, the only true means of dealing with this form of entertainment is through regulation.

The IGC has commenced implementation of the SOA by targeting a few of the longer serving IGC members with proven good standing. The application fee is to be waived for applicants of good standing with the IGC as at May 31, 2000. An annual license fee of US$2,500 will apply, while each additional registered web site will be liable for an application fee of US$250 and an annual license fee of US$250.

Through word-of-mouth and traditional advertising, the IGC intends to expand the program to include many of its member companies. Eventually, the program will be expanded to include other companies involved in the Internet gaming industry in addition to operators, such as software companies and information portals.

For further information on the Seal of Approval program please do not hesitate to contact Rick Smith or Keith Furlong at executive.director@igcouncil.org or keith.furlong@igcouncil.org respectively.

APPENDIX D

Interactive Gaming News

www.igamingnews.com

Online Gaming Jurisdictions

(Reprinted from www.IgamingNews.com)

Africa (4)

Anjouan
Liberia
Mauritius
Swaziland

Australasia (13)

**Australian Capital Territory
*Cook Islands
**New South Wales, Australia
New Zealand
**Norfolk Island, Australia
**Northern Territory, Australia
**Queensland, Australia
Solomon Islands
**Tasmania, Australia
*Vanuatu
**Victoria, Australia
Vietnam
**Western Australia

Caribbean (9)

*Antigua and Barbuda
*Dominica
Dominican Republic
Grenada
Jamaica
*Netherlands Antilles
*St. Kitts and Nevis
St. Vincent
Trinidad

Central America (3)

*Belize
*Costa Rica
*Nicaragua

Europe (19)

Åland
Alderney, UK
Austria
Belgium
Faroe Island (Denmark)
Finland
France
Germany
*Gibraltar, UK
*Great Britain, UK
Iceland
*Ireland
*Isle of Man, UK
Liechtenstein
*Malta
Norway
Scotland
Spain
Sweden

The Far East (4)

Hong Kong
Macao
Singapore
The Philippines

North America (5)

*File Hills, Saskatchewan (Canada)
*Mohawk - Kahnawake (Canada)
Louisiana (USA)
Oregon (USA)
Pennsylvania (USA)

Russia (1)

*Kalmykia, Russia

South America (3)

Chaco (Argentina)
Formosa (Argentina)
Venezuela

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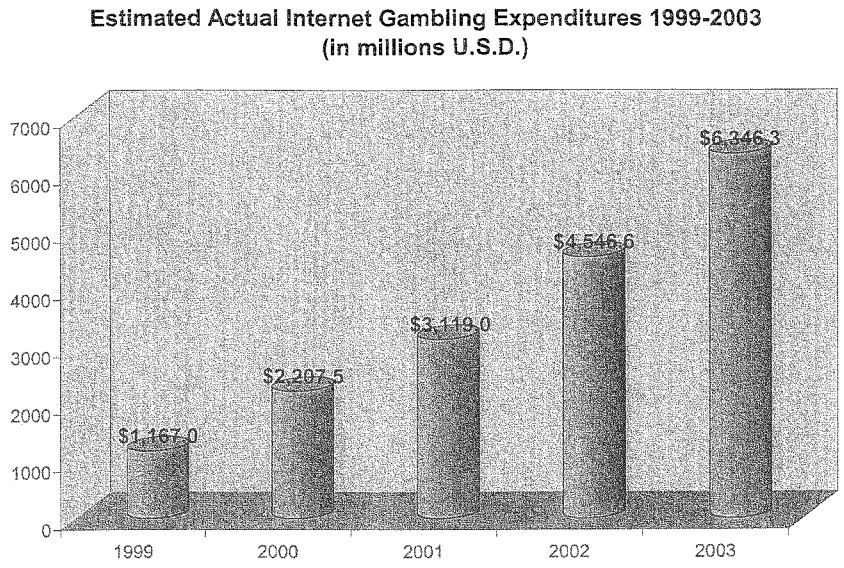
*To our knowledge these jurisdictions are currently accepting applications.

**Note: In June 2001, Australia's Senate passed a law that prohibits Australian Internet casinos from accepting bets from Australian residents as well as from bettors in any country with a similar law in place.

July 10, 2001

APPENDIX E

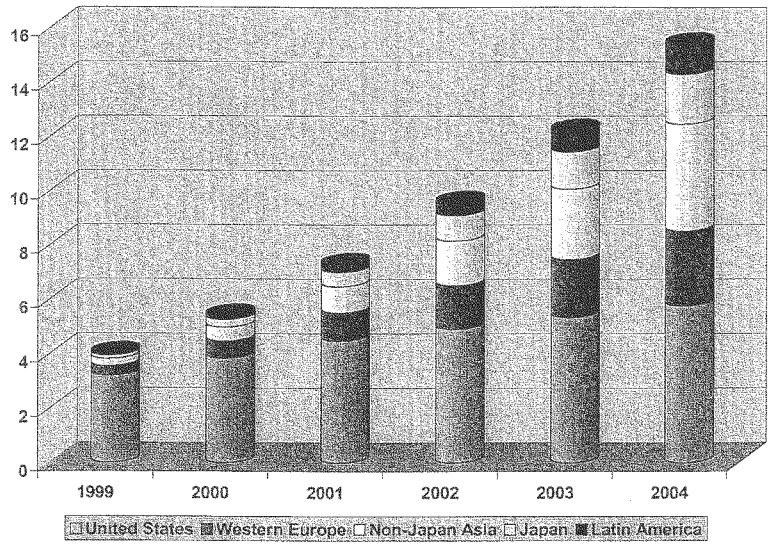


Source: Christiansen Capital Advisors, LLC

APPENDIX F

SECTION 4:

Figure 4.3 Geographic Breakdown of Internet Gambling Players 1999 to 2004 (in millions)



Source: Christiansen Capital Advisors, LLC

Responses to Representative Luis Gutierrez Questions on Internet Gaming

1. What measures does the council use to corroborate that customers accessing gaming systems are of lawful age?

2. Under the Council' s Responsible Gaming Guidelines, regarding controlling compulsive gambling, what's "the proposed loss limit for customers?"

3. What kinds of sanctions can the council use to insure compliance with all requirements of law and to punish non-law abiding people?

These three questions can be answered comprehensively together:

In response to the questions above, it is important to note that the Interactive Gaming Council (IGC) was never intended to be a regulatory body and/or usurp the role of governments with regard to the regulation of gaming over the Internet. Further, growth statistics and revenue projections as presented for the Internet gaming industry imply that a percentage of monies are from our citizens and leave the United States with no subsequent benefit, directly or indirectly, to the U.S. (including no dedicated funds for protecting children and problem gamblers through education or other programs).

The Interactive Gaming Council (www.igcouncil.org) is an international non-profit trade association of over 100 companies around the globe that are involved with the interactive gaming industry. As a non-profit trade association, the IGC has no legislative authority to place sanctions on its members or "non-law-abiding" people.

The IGC's mission is to: provide a forum to address issues and advance common interests in the global interactive gaming industry; establish fair and responsible trade guidelines and practices that enhance consumer confidence in interactive gaming products and services, and serve as the industry's public policy advocate and information clearinghouse. An important role of the Interactive Gaming Council is to advocate for the adoption of strong government regulation of the Internet gaming industry throughout the World. To achieve this end the Council actively promotes cooperation within, and between, industry and government.

In land-based gaming, jurisdictions devote significant resources to preventing minors from gambling. Obviously, the physical presence of minors helps to facilitate their identification. Yet, even with the opportunity presented by the physical presence of minors, no gaming jurisdiction is 100% effective in keeping minors from gambling. By

contrast, many tools, including data cross checks and age verification software, are currently available to exclude minors from participating in gambling online. The IGC contends that stringent computerized screening mechanisms implemented by Internet gambling operators, and monitored by regulators, will be more effective than existing land-based measures in preventing most minors from gambling. With new technologies there is the need for a stringent registration process for players wishing to participate in interactive gambling. Coupled with this should be equally stringent verification procedures for each time a person wishes to participate in any form of gambling. New technologies actually provide regulators with tools not previously available in most traditional forms of gambling, including the ability to provide an audit trail for each transaction, to limit players to total or individual amounts bet, and to block participation by specified players or classes of players, such as college athletes.

Similar resources are devoted to protect problem gamblers in the traditional gaming industry. In our opinion, it is possible that a computer-based system that allows a gambler to self-exclude or to establish loss limits stands a far greater chance of being effective than the systems in place in most casino jurisdictions today. In fact, computer technology provides an opportunity to identify patterns of behavior that may lead to problem gambling, and offer intervention in a more timely and critical manner. Sure, a gambler who is determined to gamble can move from Web Site to Web Site, but a gambler who is determined to gamble could move from one form of land-based gaming to another, including government-run lotteries.

In our humble opinion, if the U.S. government wants to provide protection for the public, especially children and compulsive gamblers, then the answer is regulation. An outright ban on Internet gaming as proposed in past sessions of congress will only stop U.S. companies, or companies with a nexus to the U.S., from participating in the Internet gaming industry and providing gaming to U.S. consumers. Regulation, on the other hand, is the best way to protect consumers and to ensure that a well-regulated, safe and fair alternative is available. The sooner governments and Internet gaming operators realize the need for regulation, the quicker that fly-by-night operators or those operators with organized crime and other unsavory backgrounds, will be put out of business.

4. How can regulators assure themselves that the "prototype" Internet gambling computer program is safe from tampering by operators or hackers?

5. How can the Internet gambling operation protect the confidentiality of bettors' financial information from internal or external misuse?

As with any form of e-commerce, good business practices, security technology and internal controls should be in place to ensure transaction integrity, the security of the site and the privacy of information. These same philosophies underpin any form of business.

Regulations would have to be drafted requiring strict internal audit procedures for the operation of gaming sites. Approved licensees, both corporate and individual, should be

required to adopt a comprehensive set of internal controls with proper records being kept for review by regulators. The regulator should have the ability to review periodically, and randomly, the gaming records of each licensee to ensure the financial responsibility of the licensee and fairness of the games being offered.

The Interactive Gaming Council promotes the regulation of Internet gaming in a cooperative framework in order to provide a fair and honest environment for participants and operators alike. Again, strict government regulation is a necessary ingredient toward fair and honest on-line gambling, as is the evaluation of games against agreed standards.

The same level of scrutiny that exists in traditional forms of gaming needs to apply to the evaluation of systems and games and to the general good business practices and internal controls addressing the operational and administrative processes. For example, in land-based gaming jurisdictions, slot machines and other electronic games are tested to assure compliance with regulated standards before a single machine can be placed on a casino floor.

Licensed Internet gaming sites should be "industrial strength" and comply with the highest technical requirements that current technology will provide, similar to requirements adhered to by banks and other financial institutions. Continuous inspection by gaming agents is an essential requirement. Inspections at the server location of the hardware and software will occur randomly and online testing should determine that the games being offered to the public are the same as the original program approved by the regulators. Inspections and continuous monitoring would assure consistent compliance with technical requirements.

Miscellaneous IGC Programs

I would like to take the opportunity to briefly overview two important programs created by the IGC to assist in its mission: the Code of Conduct and the Seal of Approval Program. All members of the IGC agree to adhere to the IGC Code of Conduct as a condition of membership. With the changing composition of the IGC membership and the flexible, evolving nature of a document such as a Code of Conduct, the IGC recognizes the need for this document to be constantly subjected to review. As the IGC has evolved, the organization has recognized the need to provide industry members with an accreditation that the public will recognize and trust. The Seal of Approval program allows operators to display a seal that indicates to consumers the site's willingness to adhere to a new, higher level of compliance as a supplement to existing government regulatory regimes.

The Seal is an actual logo that is placed on interactive gambling site to symbolize a willingness of the operator to adhere to a higher level of integrity and responsibility. The Seal of Approval logo is currently served from a dedicated third party server in order to protect, to the best of our technical abilities, its authenticity and to allow for instantaneous removal of the seal should the IGC revoke its approval.

While there are no guarantees, the IGC believes that the Seal of Approval program is an important step toward increasing the legitimacy of the Internet Gaming Industry. The IGC and its programs are by no means designed to be a replacement for strict government regulation. In fact, the IGC position is that effective government regulation is the only way to move the Internet gaming industry, as a subset of eCommerce in general, to the next level of legitimacy.

Responses to questions from Rep. Sue Kelly:

1. Many believe that current law, including the Wire Act, makes Internet gambling illegal already. Do you agree with this interpretation of Federal law?

Well, I should begin by saying that I am not a lawyer, so I can't give an interpretation so much as some impressions gleaned from things others have said.

The question "is Internet gambling illegal" begs several questions. There are several types of Internet gambling, including sports-book, casino-style, pari-mutuel (and subdivisions thereof such as horse racing, dog racing, etc.) lottery, and player-versus-player style games. These all have varying degrees of legality.

Then there is the question of state law, and from which state the wager is placed and in which state the wager is received. If they are the same state, the Wire Act (I believe) defers to state law.

Then there is the question of jurisdiction and which laws apply. If a consumer in Virginia links through an ISP in D.C. to place a bet at a server on the Isle of Man, with a company domiciled in the United Kingdom, what laws apply. A fundamental question for all e-commerce transactions is, "where does the transaction occur?"

A few things seem reasonably settled. Wagers received in Utah, Hawaii and Tennessee are definitely illegal, whether they use the Internet or not. Interstate sports-book wagers over the Internet, received in the United States are probably illegal, as are most intrastate sports wagers outside of Nevada.

I believe the Wire Act has at least once been interpreted as not governing casino-style gambling, but many state laws would prohibit the acceptance of such wagers in those states. IGC has not focused on pari-mutuel or lottery wagering on the Internet, but I am told both have some legal grayness to them.

The question of how and whether U.S. law governs wagers placed over the Internet to offshore sites is not resolved. The U.S. Department of Justice has stated its position that such wagers are violations of U.S. law, and within U.S. jurisdiction, but that position seems at odds with positions the U.S. has taken in comparable matters, such as the France/Yahoo case, as I understand it.

In short, there are too many variables to answer the question succinctly, but I do not believe the law is well-settled in this area.

2. How much of the commercial business conducted by the members of the IGC is with offshore Internet gambling operations in the Carribean and elsewhere?

IGC has limited access to the information requested in this question. We do some scrutiny of our members' businesses as part of our due diligence process before allowing them to have the IGC seal on their site, but we do not aggregate data, nor do we retain records of this. I can tell you that the majority of Internet gaming is conducted by offshore operators, and that we have offshore operators among our members.

I can tell you with a fair degree of certainty that it is a substantial amount of business, but in terms of percentages, I do not have the information.

Testimony of Penelope W. Kyle
President, North American Association of State & Provincial Lotteries
Executive Director, Virginia Lottery
July 12, 2001

Good morning Madame Chairwoman. My name is Penelope Kyle and I am the President of NASPL—the North American Association of State & Provincial Lotteries, as well as the Executive Director of the Virginia Lottery. I greatly appreciate the opportunity to testify before you this afternoon regarding your interest in Internet gambling. I come here today, not to represent the Virginia Lottery, but rather to act in my official role as spokesperson for NASPL, which represents the interests of lotteries in 38 states and the District of Columbia, in addition to the Canadian Provincial Lotteries, the Virgin Island Lotteries, the Jamaican Lottery and the Lottery in Puerto Rico.

I should first say that NASPL applauds your committee and the other relevant congressional committees for addressing the issue of illegal and unregulated Internet wagering. As state lottery directors, our NASPL members operate under some of the most stringent legal and security standards in the world. We do this because we believe it is in our best interest if we are to maintain the high level of public trust we have gained from the citizens of our states. Therefore, your efforts to outlaw illegal Internet operations should be supported by those of us who are playing by the legal wagering rules.

It should be noted that NASPL does not have a "for or against" position on Internet gambling. It is the position of NASPL that each individual state should determine the regulation of forms of gaming, as well as the methods in which they are offered to the citizens of that state. My goal in coming before your committee today is to make one key point to members of Congress: NASPL would not support any Internet legislation that would preempt the right of the nation's governors and state legislators to authorize and regulate gaming within their borders. Since the inception of the New Hampshire Lottery in 1964, state governments have held the right to authorize and regulate their state lotteries, raising billions of dollars for good causes such as education, the environment and senior citizen programs.

NASPL stands in agreement with the National Governors' Association, which has written:

"States possess the authority to regulate gambling within their own borders and must continue to be allowed to do so. An incursion into this area with respect to online gambling would establish a dangerous precedent with respect to gambling in general as well as broader principles of state sovereignty."

It should be noted that there are several state lottery members of NASPL who are opposed to offering state lottery games over the Internet. These states feel strongly about this issue and would oppose any attempt to authorize such games. On the other hand, there are some NASPL state lottery members who feel that there may come a time in the future when it is appropriate to offer such games. I make this point, Madame Chairwoman, to illustrate an important common theme among our membership: we may not all agree on the value or appropriateness of Internet lottery games, but we ARE united in the belief that it should be clearly a state's right to authorize and regulate its own lottery.

In conclusion, I would ask that this committee and other relevant committees respect the historical right of states to authorize and regulate gaming within their own borders.

Madame Chairwoman, I thank you again for allowing me to offer these views and opinions on behalf of the North American Lottery Industry.

August 10, 2001

Mr. Hugh Nathanial Halpern
Parliamentarian and Director of Legislative Operations
U. S. House of Representatives
Committee on Banking and Financial Services
2129 Rayburn House Office Building
Washington, D. C. 20515

Dear Mr. Halpern:

I am responding to the question submitted by Congressman Luis Gutierrez concerning my testimony at the July 12, 2001 hearing on internet gambling held by the Subcommittee on Oversight and Investigations.

It is our opinion that the problem of illegal Internet gambling can be addressed under current law. This opinion is based on current state laws that prohibit certain gambling activity occurring in each state and current federal law (The Wire Wager Act, 18 U.S.C.§1084). State and federal law enforcement officials have successfully prosecuted a number of cases against operators of illegal Internet gambling. The following are examples of cases that have already been or currently are being adjudicated:

State Attorneys General have prosecuted cases under state law, both criminal and civil, against operators of illegal Internet gambling. The Attorneys General in Minnesota, Missouri, and Wisconsin have successfully argued that since a part of the Internet gambling was taking place in their states, namely that the wagers or bets were placed by persons that were physically located in their states, that state's gambling laws which make such gambling illegal applies. In each of those states the courts have held that the state had jurisdiction over the operator of the illegal Internet gambling (even though the operator was located in another state).

The U. S. Attorney in New York filed criminal charges against a number of individuals conducting illegal Internet gambling in the United States. The U. S. Attorney stated that federal law clearly prohibits anyone engaged in the business of betting or wagering from using interstate and international wire communications including the Internet. One of the individuals charged, Jay Cohen, was convicted last year of conspiracy and substantive violations under The Wire Wager Act. The 2nd Circuit Court of Appeals upheld that conviction on July 31, 2001.

State Attorneys General have stopped the Coeur d'Alene Indian Tribe in Idaho from operating a National Indian Lottery that was planning to use the telephone and the Internet for the placing of bets. The Federal District Court in Idaho stated that the fact that the act of ordering a chance in the lottery was to occur in another state makes the gambling activity subject to that state's gambling laws. This case is currently on appeal to the 9th Circuit Court of Appeals.

If you need any additional information, please contact me.

Very truly yours,

Penelope W. Kyle

August 31, 2001

Mr. Hugh Nathanial Halpern
Parliamentarian and Director of Legislative Operations
U. H. House of Representatives
Committee on Banking and Financial Services
2129 Rayburn House Office Building
Washington, D. C. 20515

Dear Mr. Halpern:

I am responding to the questions submitted by Congresswoman Sue Kelly concerning my testimony at the July 12, 2001 hearing on Internet gambling held by the Subcommittee on Oversight and Investigations.

1. **Many believe that current law, the Wire Act, makes Internet gambling illegal already. Do you agree with this interpretation of Federal law?**

   It has become clear that the current law governing "wire wagering" is ambiguous, at best. There are some legal opinions that say the 1961 Wire Wager Act applies to the Internet, while other opinions say the law does not apply to the Internet. In short, there needs to be some clarification and universal law relating to the Internet and wagering.

   However, any new laws must be careful to not infringe upon the historical right of states to regulate gaming within their borders. Even with the Internet, states should be able to regulate that form of gaming, as it applies to currently *legal* forms of wagering within a respective state. Furthermore, states should be allowed to reserve the right to offer *legal* internet wagering in the future, only after they can prove that the safeguards are in place to prevent unauthorized or underage wagering.

2. **Does the NASPL believe that under new State laws, like that just passed in Nevada, Internet gambling operations could be lawfully established in the United States?**

   NASPL does not take a position on an action taken by a state legislature that affects only that state. What is clear is that there is a demand for this sort of wagering, and states like Nevada are following their historical role of regulating gaming within their borders by passing new Internet wagering legislation. Nevada lawmakers have clearly decided that Internet wagering is a form of gaming that they may want to explore in the future, but only after it is authorized and regulated by an oversight board *and* can be proven to be feasible by preventing unauthorized or underage wagering.

3. **Do State lotteries oppose legislation introduced by Representative Leach that would prohibit gambling businesses engaged in unlawful gambling from accepting bank instruments?**

   NASPL does not oppose the current draft of the Internet funding prohibition legislation, introduced by Congressman Leach. In fact, we welcome legislative efforts to curb *unlawful* Internet wagering, the original genesis of all Internet wagering legislation.

4. **The National Association of Attorneys General has expressed support in the past for Federal legislation on Internet gambling because it is, by its very nature, "interstate" and thus not well suited to State law only. The National Gambling Impact Study Commission, in its 1999 report, also recommended that Internet gambling be handled at the Federal, not State level. Yet, in your statement, you state that the NASPL and the National Governors Association both support State**

control over online gambling. As a practical matter, how can States adequately police online gambling given the interstate nature of the Internet?

As technology develops, there will come a time in the future when lotteries authorized by their states will be able to prevent unauthorized and illegal (i.e., out-of-state and underage) access to their state lottery sites. This technology will allow state lotteries to sell their products within their state boundaries only.

No one could have ever predicted the explosion and revolution that has come with the Internet; would anyone have thought 10 years ago that you could buy everything from groceries to automobiles over the Internet? I make this point to emphasize that *legal* state lotteries, who mission it is to raise funds for good causes, should be allowed to preserve for the future the option of distributing their products intrastate via the Internet if the above safeguards can be demonstrated.

If you need any additional information, please contact me.

Very truly yours,

Penelope W. Kyle

TESTIMONY OF GREGORY C. AVIOLI
DEPUTY COMMISSIONER AND CHIEF OPERATING OFFICER
THE NATIONAL THOROUGHBRED RACING ASSOCIATION
to the
OVERSIGHT AND INVESTIGATIONS SUBCOMMITTEE
HOUSE FINANCIAL SERVICES COMMITTEE

July 12, 2001

NATIONAL THOROUGHBRED RACING ASSOCIATION
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TESTIMONY OF GREGORY C. AVIOLI
DEPUTY COMMISSIONER AND CHIEF OPERATING OFFICER
THE NATIONAL THOROUGHBRED RACING ASSOCIATION
to the
OVERSIGHT AND INVESTIGATIONS SUBCOMMITTEE
HOUSE FINANCIAL SERVICES COMMITTEE

July 12, 2001

I appreciate this opportunity to present the views of the horse industry on the financial aspects of Internet gaming as it applies to the pari-mutuel horseracing industry.

I am testifying today in my capacity as Deputy Commissioner and Chief Operating Officer of the National Thoroughbred Racing Association (the "NTRA"). The NTRA is the national organizing body of the sport of Thoroughbred racing representing the interests of the majority of racetracks, owners and breeders in the United States.

THE PARI-MUTUEL RACING AND BREEDING INDUSTRY

Pari-mutuel horseracing, including off-track and inter-track wagering is legal in 43 states and involves the racing of Thoroughbreds, Standardbreds, Quarter Horses, Arabians, Appaloosas and Paints. There are over 175 racetracks in the U.S. Racing and racehorse breeding is a widespread and diverse industry that includes sports, legal wagering, recreation and entertainment and is built upon an agricultural base that involves the breeding and training of the horses.

Economic Impact

According to the "Economic Impact of the Horse Industry in the United States," a study done by Barents Group, LLC, the economic and fiscal consulting unit of KPMG Peat Marwick LLP, for the American Horse Council Foundation, racing and racehorse breeding have a total economic impact in the U.S. of $34 billion and generate 472,800 total full-time-equivalent jobs. There are 941,000 people and 725,000 horses involved in the racing industry.

Wagering on horseracing is permitted in 43 states and there is an active horse breeding and training business in all 50 states. In many, the economic contribution of the racing and breeding industry to state and local economies is substantial and the industry ranks among the state's most significant economic entities. For example, in New York, it involves 45,000 horses, has a $2.6 billion economic impact and generates 33,600 full-time job equivalents; in Florida, it involves 37,000 horses, has a $2.1 billion economic impact and generates 27,300 full-time equivalent jobs; in California it involves 69,000 horses, has a $4.1 billion economic impact and generates 52,000 FTE jobs; in Illinois, it involves 52,000 horses, has a $2 billion economic impact and generates 30,700 FTE jobs; in Ohio, it involves 40,000 horses, has a $1.3 billion economic impact and generates 17,000 FTE jobs; and in Texas, it involves 74,000 horses, has a $1.8 billion economic impact and generates 27,900 jobs.

Pari-mutuel racing generates over $500 million annually in direct state and local revenue from pari-mutuel taxes, track licenses, occupational licenses, admission taxes and miscellaneous fees.

Racing as a Sport

Racing is an activity that attracts millions of fans who appreciate it and follow it as a sport and who enjoy the excitement of the race and the athletic ability of the horses. The Triple Crown and Breeder's Cup World Thoroughbred Championship races are considered among the most important sporting events conducted in the United States each year and are widely reported in the sports media. Over 160 additional hours of top Thoroughbred races are broadcast on national television each year, on networks including NBC, CBS, the ESPN networks, and CNBC. The national championships of Standardbred and Quarter Horse racing are also televised nationally and widely covered by the media. In addition, most major U.S. newspapers cover racing and print the results of the races at their local tracks on a daily basis, much like they print the box scores of other sports.

The Pari-Mutuel System

While horseracing is a sport on which one can gamble, it would be erroneous to assume that pari-mutuel wagering is the same as other forms of gambling. Unlike most other forms of gambling, horseracing uses the pari-mutuel system in which bettors wager against one another instead of against the "house." Of the total amount wagered on a particular race, approximately 80% is returned to winning bettors. The other 20%, called the "takeout," is shared between the state government, the racetrack and the horsemen who race at the track. Takeout rates, which vary from state to state, are published in track programs, which are available at race tracks and at simulcast wagering sites away from the track, so that fans know the rates and how they might affect their wagering.

Wagering computations are accomplished by a totalisator machine, a computer, that adds bets over and over again during the course of betting. Every 30 to 60 seconds the "tote" flashes new betting totals and odds for each horse. The machines contain a number of features designed to minimize the potential for pari-mutuel fraud or machine malfunction. These features include coded ticket paper and duplication of all critical functions by two computers working independently of one another.

I point this out because the pari-mutuel system and the published information available ensure that the public has easy access to data regarding the wagering odds. The use of the tote machine allows bettors to determine the betting odds every 30 to 60 seconds. In addition, the race upon which the wager is made, and paid, is a public event, watched by fans at the track or off-track facility, often viewed by others on television or cable, and always overseen by the stewards at the track itself and the state racing commission to ensure the integrity of the race.

In 2000, over 30 million people attended the races and wagered over $14 billion, approximately 80% of which was returned to the winning players.

CURRENT ACTIVITIES OF RACING

The dissemination of information about racing, simulcasting, account wagering and commingling of pari-mutuel pools have been ongoing activities conducted by state-licensed entities for many decades. These activities, which in today's modern world are now heavily dependent on the use of computer networks and, in many cases the Internet, are the primary revenue-generators of the racing and breeding industry.

Information

Like other businesses, we live in a highly complex and ever-changing technological world. In this environment new industries have sprung up virtually overnight forcing existing industries to adapt and change practices in order to compete for the public's support. This is particularly true in the areas of wagering and entertainment.

Like others, the horseracing industry has had to adapt and change dramatically in the face of exploding competition and new technology. An example of that is that many racetracks, horsemen's associations and private businesses are now advertising and offering information on the sport through various media, both traditional and more technological state-of-the-art, including the Internet.

The process of betting on horse racing and selecting the winner is called "handicapping." It is a cerebral process for serious bettors that spend a great deal of time at the track, and elsewhere, pouring over information that will help them select the winners of races. For students of the sport this is not a random selection. The "handicapping" information used in this process has been available in written form since racing began and is similar to the statistical information available for other sports.

The racing industry is presently offering a great deal of this type of "handicapping" information in publications, on-the-wire, over toll-free numbers and over the Internet in the form of advertisements for state-licensed and regulated race tracks, information and "how-to" sites, "tout" sheets, past performance information, betting lines and similar information, that will market the racing product to new fans and allow existing patrons to participate more successfully.

This continued flow of this information is critical to the racing business and we submit should not be affected by any changes to current law.

Simulcasting and Account Wagering

Prior to 1970, legal pari-mutuel wagering on racing was limited to those at the track where the race was run. In 1970, the New York legislature approved off-track wagering. As an aside, at that time the computerized system operated by New York OTB (Off-Track-Betting) was one of the first real-time, on-line computer systems in the U.S. Since then, many states, and the federal government under the Interstate Horseracing Act of 1978, have authorized racetracks to simulcast or transmit signals of their races off-track into other states and jurisdictions ("interstate simulcasting") under applicable law.

With the continued development of technology, by the early 1980s racing was able to further improve its product by electronically linking pari-mutuel wagering pools among tracks in separate jurisdictions through a sophisticated computer network (a process known as "commingled pools" or "common pooling") so that payouts could better reflect the size and wagering behavior of the entire betting public.

The racing industry's continuing utilization of state-of-the-art technology has resulted in the ability of the industry to survive and offer its patrons a better product. In fact, today over eighty percent of the money wagered on racing is bet at facilities or locations other than where the race itself is run. Again, all with the approval and regulation of the states involved.

Another process for pari-mutuel wagering on racing that has expanded over the two last decades is account wagering, whereby an account holder establishes an account with a licensed account wagering facility and is able to send instructions to place wagers from that account via telephone or other electronic means without being physically present at the facility. Currently, eleven states, including Connecticut, Kentucky, Louisiana, Maryland, Nevada, New Hampshire, New York, Ohio, Oregon, Pennsylvania and South Dakota, have enacted legislation specifically authorizing the acceptance of account wagers by licensed facilities within those States and a number of others are considering similar legislation.

Account wagering is not a new activity in the United States. Telephone account betting has been offered in New York for over 25 years by New York City Off Track Betting and upstate New York Off Track Betting entities-- all state agencies. These entities have accepted wagers from residents of New York and other states who had established accounts in New York.

In order to keep pace with modern technological advances, the horseracing industry needs to be able to continue these activities, provided that such activities are conducted in accordance the Interstate Horseracing Act of 1978 and applicable state laws or regulations.

FEDERAL AND STATE POLICIES ON PARI-MUTUEL WAGERING ON HORSERACING

Gambling, including that conducted on horseracing, has always been of concern to the federal and state governments. Throughout American history, the prohibition or legalization and regulation of gambling has primarily been a function of the states. The only time that the federal government has become involved has been when one or more states could not solve a problem without federal intervention. But even in these instances, for the reasons discussed above and others, pari-mutuel racing has often been either treated differently or specifically considered under federal gambling laws. The racing industry has developed to its current status under a regulatory framework of state law and regulation and the Interstate Horseracing Act of 1978. In order for the racing and breeding industry to continue to compete in today's economy, it must be able to continue to do so under these same statutes.

State Regulation - A Long History

Pari-mutuel racing has been conducted in the United States under state authority and regulation for over 75 years. In every state that has allowed legalized wagering on horseracing,

strict state oversight and regulation has accompanied its introduction and growth. In each state the pari-mutuel industry is regulated by an agency most commonly known as the state racing commission. Among commission prerogatives are the licensing of track and horse owners, trainers, jockeys, drivers and all others involved in the pari-mutuel sport, and the promulgation and enforcement of the specific regulations under which the industry must operate. All matters pertaining to the operation of pari-mutuel racing, including wagering, are regulated by these agencies on behalf of the governors and state legislatures.

Over the years the states have consistently acted on the perceived need to closely regulate legal wagering and protect the public's interest in pari-mutuel sports. The actions of state legislatures and the racing commissions that carry out their policies have been predicated on the desire to: (1) determine whether to allow pari-mutuel wagering on horseracing within their borders; (2) maintain the integrity of the events on which the public is allowed to wager; (3) oversee the state's tax-related and economic interest in that wagering; (4) ensure that licensees meet specific standards of qualification; and (5) control any unsavory elements which may attempt to associate with the wagering aspects of the sport.

The Interstate Horseracing Act of 1978

In 1978, Congress enacted a federal statute that specifically deals with interstate gambling on horseracing. The Interstate Horseracing Act of 1978 ("IHA") made clear that a racetrack controlled wagering on its races in interstate commerce and provided for industry and regulatory approvals before betting was permitted between jurisdictions where the wagering was legal.

In the findings to the IHA, Congress said that states have the primary responsibility for determining what forms of gambling may take place within their borders, but that the Federal government should prevent interference by one state with the gambling policies of another. In the IHA Congress provided that with respect to the limited area of interstate off-track wagering on horse racing:

> There is a need for Federal action to ensure that States will continue to cooperate with one another in the acceptance of legal interstate wagers.

Importantly, in passing the IHA, Congress specifically recognized that "pari-mutuel horseracing is a significant industry which provides substantial revenue to the States" and that "properly regulated and properly conducted interstate off-track betting may contribute substantial benefits to the States and the horseracing industry."

Consistent with these findings, Congress stated as a matter of congressional findings and policy that:

> It is the policy of Congress in this chapter to regulate interstate commerce with respect to wagering on horseracing, in order to further the horse racing and legal off-track betting industries in the United States.

For more than twenty years the combination of state statutes and regulations and the IHA provided the racing industry with a workable regulatory framework that has allowed the industry to develop its current activities within clear parameters and guidelines.

During consideration of the Internet gambling bills in the last Congress, however, the Department of Justice took a new and unexpected position regarding the legality of the long-standing activities of the horseracing industry we have described above. In opposing a provision in the Internet Gambling Prohibition Act of 1999, H.R. 3125, which grandfathered certain forms of licensed pari-mutuel wagering from the prohibitions of the Act, a Deputy Assistant Attorney General in the Department of Justice questioned, for the first time, the legality of interstate simulcast wagering, commingling of pools and account wagering under the Federal Wire Act (18 USC 1084).

Because these long-standing, state-sanctioned activities account for a substantial majority of the revenues for the horseracing and breeding industry, this unprecedented position by the Department of Justice put at risk the ongoing viability of the $34 billion horseracing and breeding agribusiness. The activities questioned had been openly offered for decades in many states in compliance with state law, the regulation of the state racing commission and the IHA. For example, New York has offered interstate account wagering through its state-owned off-track wagering facilities for decades under the regulation of the New York Racing and Wagering Board and the New York Attorney General since the early 1970s.

Our industry made significant efforts to communicate to the Justice Department and Congress that the new position was an extreme and incorrect interpretation of the Wire Act and was contrary to the language and spirit of the IHA -- enacted seventeen years after passage of the Wire Act-- for the express purposes of ensuring proper regulation of "interstate off-track betting" and "furthering the horseracing and legal off-track betting industries in the United States."

Fortunately, Congress agreed with our position and concern and amended the IHA last year to clarify that simulcasting, account wagering and commingling of pools may be conducted on an interstate basis where lawful in the States involved. This amendment to federal law did not expand any wagering activities, which as noted have been ongoing for decades, and did not override any state laws regulating, permitting or prohibiting such wagering.

THE INTERNET GAMBLING ISSUE

The regulation of all forms of gambling is essential to protect the public and ensure compliance with applicable federal and State laws. Our industry is opposed to any unregulated or unauthorized gambling, particularly on racing. Accordingly, over the past few years, we have supported various measures in Congress designed to prevent illegal, unregulated Internet gambling, including The Internet Gambling Prohibition Act of 1999, where such legislation included appropriate provisions that would allow horseracing to continue to conduct its existing activities using modern technology.

As a result of participating in this legislative process, we are aware that any legislation dealing with Internet wagering will involve very complicated legal and technical issues and are concerned that imprecisely or improperly drafted legislation may adversely impact activities the

racing industry is currently conducting under state regulation and the IHA with respect to the dissemination of information, interstate simulcasting, commingling of wagers and account wagering.

The worst possible result for all concerned would be to enact legislation that would restrict licensed and regulated entities from conducting their current business using modern technology with the result being that many of those who wish to wager on horseracing will be forced to deal with unlicensed and unregulated vendors, either off-shore or operating illegally within the United States. This would open the door to consumer fraud and result in significant decreases in revenues for the licensed operators, purses (which are directly derived from licensed wagering revenues) and tax revenues for the Federal and State governments.

It is critical to the future of the racing industry, the agri-business it supports, the state revenue and employment it generates, the sporting and the entertainment benefits it provides to countless fans, that modern distribution mechanisms of racing information and its product be available, so long as they continue to meet regulatory criteria established by state governments and comply with the IHA. It is also critical that the racing industry have the opportunity to take advantage of any and all technological advancements in the future distribution of its information and products in order to successfully compete against other forms of gambling, sport and entertainment.

Because of the unique status of racing and breeding industry as a major United States agribusiness supporting hundreds of thousands of full time jobs in over 40 states and the longstanding regulatory structure applicable to it, we believe that any legislation in the area of illegal Internet gambling must give appropriate consideration to our industry. Any such legislation should maintain the effective framework of state and federal regulation of pari-mutuel horseracing and the current protections offered to the public through this well regulated system and respect the longstanding federal policy to allow individual states primary authority over wagering issues within their respective states. We look forward to working with the members of Congress to accomplish this result.

Dear Chairwoman,

I refer to your July 12th hearing "The Financial Aspects of Internet Gaming - A Good Gamble or Bad Bet?"

I am a bookmaker and as a member of its Internet Betting Committee I represented the Australian Registered Bookmakers' Advisory Council "ARBAC" during the recent passage of the Interactive Gambling Bill 2001 - now have received Royal Assent it is Act 84/2001.

While it may not seem immediately logical ARBAC, and the Australian Racing Board, actually supported the Government in its endeavour to prohibit online gaming (as against wagering).

Our argument was that wagering is not by its nature "interactive" and therefore given other legislation encouraging e-commerce, an online wagering transaction which is no different to a face to face, or telephone, bet should not be captured. We did agree with the Government though that there where developments occurring, particularly in iTV technology, that facilitated "interactive wagering" or "micro-event wagering" that were gaming-like in nature and should therefore also be banned. This was the final result.

I was privileged to work very closely with the cross bench Senators in drafting various amendments; including the need for later finessing by regulation, unenforceable contracts and the reciprocality provision - the so called "Good Neighbour" amendment. Without these amendments to the Government Bill it would not have secured the necessary 4 cross bench votes (it actually got 6).

Contrary to some views, pushed largely by those aligned (read self-interested) with online gaming, there is no doubt that this is good legislation. Polling of the Australian people found that 80-90% favoured this measure, and as such it was a disappointment that the Opposition did not engage in the debate at all, and took a "it can't be done" attitude for political reasons. I also have no doubt that effective legislation and regulation can be introduced to effectively maintain a states sovereign right, and responsibility, in respect to gambling within its borders.

A personal perspective only, but the biggest problem facing the US in regulating the real problem - "interactive gaming" - is the whole issue of sports betting. The core thrust of the Australian legislation was not that it was NOT prohibitionist - but rather applied regulation that limited the accessibility of new gaming opportunities (but you could still use a video poker or electronic gaming machine (despite being connected by communications they were exempted because that was "physical" or "offline" gambling strictly regulated by the states). The legislation simply clearly demarked the boundaries (because some smaller Australian States/Territories thought the bigger States' tax revenues were "fair game", as well as being open to attack from offshore operators and then returned the responsibility to the States and Territories for their management of social policy. The issue (in my opinion) for the US is whether to regulate sports wagering on professional events but prohibit it on school/college/amateur events - this is a practice that exists worldwide and the legitimate operation of the legal operators effectively eradicates the undesirable illegal betting (both the products and operators).

We fully expect that Ministerial Council on Gambling will result in regulations that limit the exemption for wagering (on racing) and lotteries to apply only operators licensed by an Australian State or Territory - this was agreed to (as an amendment) but got waylaid by issues surrounding sports wagering (being a low tax, no direct beneficiary (the sport unlike racing), a fluid market (predominantly amongst professionals/(bookmakers) laying off risk) like the financial markets.

Notwithstanding our simple view is that a licence to provide a gambling service is a privilege not right, and is issued by a sovereign state cognisant of its impact and benefits (be it tax, or levies like in racing, or profit distribution eg. lotteries to education/charities). There is no global trade in gambling services, and no justification to over turn centuries of regulation of physical gambling because of "new technology".

We would appreciate the opportunity to contribute to the work for your committee, in the interest of achieving a global framework for the provision of online (as against interactive) gambling. In keeping with the Good Neighbour amendment - I think the moral is "do unto others as you would have them do unto you".

I have had a number of article/opinions published on www.igamingnews.com (part of the River City Group - Sue Schneider's organisation, who is also Chairman, Interactive Gaming Council). The link to this is http://www.igamingnews.com/articles/article_listing.cfm/2627 but in case you do not have access I attach it, and some of the supplementary material referred to therein. My apologies for attaching so much material in an e-mail direct to a busy public representative - but I am sure you will have someone on your staff who will be able to glean material from it that should help your work.

If there is anything I can do to assist you, or to have any of the material attached hereto formally considered as evidence, please do not hesitate to contact me.

Cheers Tim

Timothy J Ryan
Australian Registered Bookmakers' Advisory Council
Internet Betting Committee
7 Wharf Road
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Australia