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THE EXPANSION OF INTERNET GAMBLING: ASSESSING CONSUMER PROTECTION CONCERNS

HEARING

BEFORE THE

SUBCOMMITTEE ON CONSUMER PROTECTION, PRODUCT SAFETY, AND INSURANCE

OF THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION UNITED STATES SENATE

ONE HUNDRED THIRTEENTH CONGRESS

FIRST SESSION

JULY 17, 2013

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THE EXPANSION OF INTERNET GAMBLING: ASSESSING CONSUMER PROTECTION CONCERNS

WEDNESDAY, JULY 17, 2013

U.S. SENATE,
SUBCOMMITTEE ON CONSUMER PROTECTION, PRODUCT SAFETY, AND INSURANCE,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
Washington, DC.

The Subcommittee met, pursuant to notice, at 10:26 a.m. in room SR–253, Russell Senate Office Building, Hon. Claire McCaskill, Chairman of the Subcommittee, presiding.

OPENING STATEMENT OF HON. CLAIRE MCCASKILL, U.S. SENATOR FROM MISSOURI

Senator MCCASKILL. Good morning. Sorry that votes delayed our opening today. We are glad everyone is here, and we appreciate your attendance at this committee—subcommittee hearing.

Today we will examine the expansion of online gaming and its implications for consumer protection and law enforcement. In December 2011, the Criminal Division of the Department of Justice issued a Memorandum Opinion that removed almost any Federal prohibition to online gaming, paving the way for States to legalize online gaming within their borders.

Specifically, the Memorandum Opinion stated the scope of the Wire Act of 1961, long understood to criminalize all interstate online gaming, was limited only to prohibiting sports betting. By narrowing the scope of the Wire Act to sports, the Justice Department has liberated states to offer their in-state residents casino style online gaming.

Online poker is already up and running in Nevada and New Jersey, and Delaware residents will have access to a full slate of online casino games this fall. Many other states are also actively considering the legalization of online gaming. Given that online gambling is a potential revenue source for cash strapped state governments, I fully expect more states to move ahead with legalized Internet gambling. And as more states act to legalize Internet gambling, I expect to see states authorize interstate compacts to allow their residents to conduct cross-border wagering.

The question for today's hearing is, what will be the consequences for consumer protection? Gambling, whether it is bingo or blackjack, has traditionally been regulated at the state level, and its state-based model remains in place for online gaming. Yet

technology, along with interstate compacts, will make it incredibly easy for consumers to gamble across state lines without stepping foot outside their front doors.

Given this, does a patchwork of state laws and regulations sufficiently protect consumers from fraud? Can it prevent underage and problem gambling? Does the expansion of online gambling provide more conduits for criminal activity, such as money laundering? Worse, will terrorists be able to more readily use online gambling sites to launder money and finance their activities? These are all questions—legitimate questions—that I think Congress must ask.

At traditional brick and mortar casinos, the states have done a relatively good job of regulating gaming. However, what works on the floor of a casino in Las Vegas, Atlantic City, Biloxi, or St. Louis may not work in the virtual world of online gambling. The Internet provides anonymity to players, a luxury not afforded to criminals and fraudsters in the real world.

The anonymity of the Internet can provide minors with greater ability to illegally gamble, and it can allow easy access to individuals with gambling disorders to satiate their destructive habits. Is the current state-based regulatory regime prepared to handle all of these potential problems?

It is worth noting that while the states have played the primary role in regulating gambling, Congress has also played a critical part. In addition to the Wire Act, Congress has passed a slew of gambling laws that address racketeering, sports betting, financial transactions, and Indian gaming. Furthermore, online gaming is inherently an interstate matter. The borderless nature of the Internet does not recognize the boundaries and jurisdictions of individual states. As such, Congress has an important role to play in overseeing the expansion of online gaming.

For decades, the Wire Act was interpreted to be a Federal prohibition on Internet gambling. Virtually overnight, this legal assumption was eviscerated, and as a result, the landscape for the gambling industry and consumer protection has dramatically changed. Thus, it is entirely appropriate that Congress plays an oversight role to determine the consequences to American consumers. That is the purpose of this hearing.

I want to thank Senator Heller for working with me on holding this hearing, and I want to further thank him and his staff for all their hard work in helping the Subcommittee staff. I know how important this issue is to Senator Heller, and I want to be as helpful and as accommodating to the Ranking Member as I can be. I think this is an important subject, and I think this discussion we are going to have today is an important public policy matter.

And I will now turn it over to Senator Heller for his opening statement.

STATEMENT OF HON. DEAN HELLER, U.S. SENATOR FROM NEVADA

Senator HELLER. Good morning, Chairman. Thank you very much for holding this hearing, and I appreciate your remarks also. I want to thank the witnesses and those on the panel today for taking time out of their schedule to be with us today and for your expert testimony.

Online gambling and its implications on consumers have been an issue that Congress has focused on for over a decade. As many know, Internet gambling was accessible to U.S. consumers starting in the late 1990s and in the early 2000s. Illegal gambling on the Internet was on the verge of exploding in the United States, and for many years gambling websites were run by offshore operators, who, in defiance of U.S. law, offered online sports betting as well as casino type games, such as slots or roulette. Some operated from foreign jurisdictions, but many operated from small Caribbean countries that do nothing to protect consumers and protect minors.

This all changed in 2006 when Congress, including seven members of this committee—four Democrats and three Republicans—enacted UIGEA, the Unlawful Internet Gambling Enforcement Act, to put an end to this wagering. The law was effective, and it was effective in going after the bad guy. But it was not a perfect law. There were still some issues that needed to be addressed in the bill in order to give our Federal agencies the tools they needed to stop illegal Internet gambling.

Then we fast forward to December 23, 2011. What happened on December 23, 2011? The Department of Justice reversed its interpretation of the Wire Act. So, 50 years of precedent—50 years of precedent—was overturned. The Department of Justice argued that under the Wire Act, interstate gambling falls within the statute, even if the wire communications originate and terminates in the same state, provided the wire cross state lines at some point in the process. Because of this interpretation, all online wagering fell under the Wire Act.

With one decision, the Department of Justice effectively rendered all laws that have been on our books, put together by Members of Congress for over 50 years, that this very body passed 2 days before Christmas, and made it useless to regulate and stop Internet gambling.

The results are the floodgates are now open to states legalizing all forms of Internet gambling, such as casino games and lotteries. Five states have already acted, including the State of Nevada, and 20 more are looking to act. Patchwork state and tribal regulations have sparked a regulatory race to the bottom. States that already do not allow Internet gambling will have difficulty now enforcing their own laws. On top of that, no discussion has been had as to consumer protections—what consumer protections will be afforded, if any, under the patchwork system of state regulations.

And as we will hear from our witnesses today, due to the regulatory uncertainty created by that 2011 decision, the Internet has effectively turned into the Wild West for online gaming. Not only does it present an opportunity for criminals and terrorist organizations to launder money with transactions happening under the radar, but there are issues of cheating and identity theft without any recourse for consumers. There are also little, if any, regulatory standards required by these websites to securely ensure those who are playing the game are who they say they are, the age they say they are, and where they say they are.

I believe that technology does exist that can meet this goal either through biometrics or geo-location data, and I look forward to seeing the presentation of such technology software from one of our

witnesses today. Such standards provide protections for all consumers, particularly underage and problem gamblers. We must, however, be able to account for the ever-changing technologies of the Internet.

And finally, I believe that we need to examine whether or not law enforcement has the appropriate tools to either shut down or regulate the space. In the past, I have been vocal about my belief that law enforcement lacks the authority. Congress needs to provide clarity and guidance on these issues. If we do not, this illegal market will continue to grow where millions of consumers are put at risk, and criminals can act freely.

I firmly believe that Congress has the unique opportunity to act by updating the Wire Act and clarifying other existing statutes that govern Internet gambling before it is too late and states become dependent on this new source of revenue. I also believe that Congress should examine the merits of providing a path forward for limited federally regulated online poker. Poker, a game of skill, not a game of chance, is different than other house bank games, such as blackjack or roulette. I believe that if given the opportunity, appropriate consumer protection standards could be in place to protect American consumers, while still providing for a play of this nationally-recognized peer-to-peer game.

So with that, I again thank the Chairwoman for examining this issue today as important as it is may be to Nevada, it is to New Jersey, as it is to Mississippi, and frankly 48 out of 50 states. So thank you very much. And again, to our panelists for being here today, for your testimony and helping us better under the consumer issues that we are facing. I look forward to hearing from you. Thank you.

Senator MCCASKILL. Thank you, Senator Heller.

I welcome my colleague from Missouri. I am loathe to use the word "senior" at my age, so we try not to be senior or not senior. We just try to work together whenever we can, even though we have some policy disagreements from time to time. And I want to welcome Senator Schatz also for being here. I am happy to give each of you a minute or two if you would like to say anything before we begin with the witnesses.

STATEMENT OF HON. ROY BLUNT, U.S. SENATOR FROM MISSOURI

Senator BLUNT. I would just briefly say, Chairman, that I was in the House in 2006 when we passed the Unlawful Internet Enforcement Act. I supported it. It did lean heavily on the Wire Act and what we all thought at the time was the traditional and would be the ongoing interpretation of the Wire Act. And the new interpretation of that Act largely has opened the door, as both of you have well explained, to many unintended consequences.

A state like ours that has a lottery, whatever they decide that they may be allowed to do, but they should not be competing with offshore competitors and competitors that are unlicensed, unregistered, unregulated. And so, I am grateful to both of you for having this hearing today.

Senator MCCASKILL. Senator Schatz?

**STATEMENT OF HON. BRIAN SCHATZ,
U.S. SENATOR FROM HAWAII**

Senator SCHATZ. Thank you, Chairwoman McCaskill and Ranking Member Heller. Thank you for bringing this issue to the table.

As you all know, the State of Hawaii prohibits all forms of gambling. This ban reflects my view and the view of our congressional delegation, and most of the popular will of the state of Hawaii. And so, I am particularly interested as we assess the need for new Federal and state regulatory policies, how that is going to intersect with the state of Hawaii and our stated public policy, because as you pointed out, Madam Chairwoman, it is not going to recognize any of our statutory jurisdiction in the state of Hawaii, because people can gamble from whatever device they choose to utilize. So, this is important for the state of Hawaii, although it has not quite the nexus that it has for the state of Nevada.

Senator MCCASKILL. Thank you, Senator. I welcome our witnesses today. I will apologize now. I have another hearing that is an urgent matter for me that I will have to duck out for at some time during our proceedings this morning. It will be my intention to get—to time my leaving here so I can immediately do the questioning I need to do in that hearing, and immediately return so I will have an opportunity hopefully to ask questions. But I did not want any of you to think that if I leave before all of your testimony is finished that I am not interested and very engaged in this topic. When I leave, I will turn the Committee over to Senator Heller to chair in my absence, and I know he will do a great job at that.

We welcome Mr. Chuck Canterbury, National President of the Fraternal Order of Police—I thank you for being here—Mr. Matt Smith, President of the Catholic Advocate here in Washington, D.C., Mr. Thomas A. Grissen, Chief Executive Officer of Daon—am I saying that correctly, Mr. Grissen?

Mr. GRISSEN. That is right.

Senator MCCASKILL. And Mr. Jack Blum, an attorney from Annapolis, Maryland. Thank you all for being here, and we will begin with you, Mr. Canterbury. Welcome.

As a former prosecutor, I am always in uniform withdrawal, so I have great respect for all of you and your members, and look forward to your testimony.

**STATEMENT OF CHUCK CANTERBURY, NATIONAL PRESIDENT,
FRATERNAL ORDER OF POLICE**

Mr. CANTERBURY. Good morning, Madam Chairman, Senator Heller, and other distinguished members of this Subcommittee on Consumer Protection, Product Safety, and Insurance. It seems like there is a plethora of former prosecutors in the Senate, and we always like coming to testify before the people that we have worked with at home. And we appreciate you holding this hearing.

My name is Chuck Canterbury. I am the National President of the Fraternal Order of Police. We are the largest law enforcement labor organization in the United States representing over 330,000 rank-and-file police officers in the country. Again, thank you for having us here this morning, and we would like to share the views of the FOP on the impact that Internet gaming may have on public safety and the need to update and modernize the Wire Act.

We are in a wireless age, and it is clear that the Wire Act is an old law ill-suited to addressing our new problems. The Interstate Wire Act was enacted in 1961. Well, in 1961 we were dealing with the Bay of Pigs, the Beatles were first performing in the United States, and our current President was born. The FOP strongly believes it is time for our nation's legal framework to catch up to the technology that it seeks to regulate.

In 2006, the FOP strongly supported the enactment of the Unlawful Internet Gaming or Gambling Enforcement Act. The law did not expand or redefine any criminal activity, but it did require financial transaction providers to block and refuse transactions associated with Internet gaming. The aim of this legislation was not only to enforce the existing laws, but also to help combat the use of offshore gambling operations that launder money from other criminal enterprises.

In 2011, the Assistant Attorney General of the Criminal Division issued a Memorandum Opinion, which held that the Wire Act prohibited only sports betting and no other forms of online wagering. Overnight, the investigation of money laundering by organized crime and other unlawful enterprises became a lot more difficult.

A 2012 report by the U.S. Department of State notes that the Internet gaming industry is laundering millions of dollars through Costa Rica, which has become a bridge country used to send money to and from other nations and other jurisdictions. I think it is telling that 4 of the 11 individuals indicted by the Department of Justice for operating online gaming sites listed their residence as Costa Rica.

These 11 defendants were charged with violations of the UIGEA, and the Illegal Gambling Business Act, and the later Federal statute, which was adopted by Congress in 1970 in an effort to attack the profits of organized crime. However, the key component to this law is that there must be a state statute prohibiting the activity, which then allows the Federal Government to investigate and prosecute the case.

Because of the differences in state law, there are cases in which Federal authorities would be precluded from using the IGBA to interdict unlawful activity from being considered in offshore sites. We know this for certain: organized crime is using offshore online operations to launder their profits. We also know that terrorist organizations are or could be using the same strategies to launder funds.

According to the counterterrorist analysts at Jane's Strategic Advisory Service, there are indications that terrorists in Afghanistan have been using illegal gaming sites to launder their money. And money laundering is hardly the only threat. Millions of Americans wager regularly on offshore Internet gambling sites beyond the reach of the Federal Government. Without the authority previously provided by the Wire Act, there is no legal or regulatory framework for law enforcement to shut down this illegal activity.

These Americans will have no recourse if they become victims of fraud or other criminal acts. There is no enforcement mechanism to provide prompt and accurate payments, to prevent criminals from entering the marketplace, rigging games, taking advantage of

our children, or misusing customer identification and financial data.

The FOP is not advocating for any expansion in what online gaming activity is deemed unlawful. With changes in how the Wire Act can be used, the limitations of both the UIGEA and IGBA, law enforcement in the United States does not have the means to effectively identify and shut down these operations. I believe U.S. law enforcement can rise to the challenge and successfully attack online fraud, money laundering, and illegal gaming.

Frankly, it's ridiculous that the Federal Government continues to regulate dynamic, ever-changing technology with legislation crafted more than five decades ago. It is vital we address this issue before we fall even further behind.

Thank you very much for allowing us to be here today.

[The prepared statement of Mr. Canterbury follows:]

PREPARED STATEMENT OF CHUCK CANTERBURY, NATIONAL PRESIDENT, GRAND LODGE, FRATERNAL ORDER OF POLICE

Good morning, Madam Chairman, Senator Heller and the distinguished members of the Subcommittee on Consumer Protection, Product Safety and Insurance. My name is Chuck Canterbury, National President of the Fraternal Order of Police, the largest law enforcement labor organization in the United States, representing more than 330,000 rank-and-file police officers in every region of the country.

I want to thank you for inviting me here this morning to share the views of the Fraternal Order of Police on the impact Internet gaming may have on public safety and the need to update and modernize the Wire Act.

The 2011 Memorandum Opinion for the Assistant Attorney General of the Criminal Division in the U.S. Department of Justice held that the Wire Act of 1961 did not prohibit state lotteries from selling tickets online. It also reinterpreted the statute much more narrowly, holding that the Act only prohibited sports betting and not other forms of online wagering.

We are in a wireless age and it is clear that the Wire Act is an old law ill-suited to addressing our new problems. The Interstate Wire Act was enacted in 1961—a time when the great-grandfather of the Internet, ARPANET, was still in its embryonic stage. The FOP strongly believes it is time for our nation's legal framework to catch up to the technology it seeks to regulate.

The FOP has been very active on these issues and we have repeatedly urged the Administration and Congress to work with us to update this law and give law enforcement the tools they need to successfully investigate and prosecute these crimes.

In 2006, the FOP supported the enactment of the "Unlawful Internet Gambling Enforcement Act." This law did not address expand or redefine any criminal activity but it did require financial transaction providers to block and refuse transactions associated with illegal gambling. The aim of law enforcement in supporting this legislation was not only to enforce existing gambling laws—like the Wire Act as it was interpreted and applied at that time—but also to help combat the use of these offshore gambling operations to launder money from other criminal enterprises. It is clear from testimonies given before Congress on this issue and the new application of the statute as interpreted by the Justice Department that law enforcement needs a better, clearer framework as well as new tools if we are to achieve these ends.

Money laundering is hardly the only threat. Millions of Americans wager regularly on offshore Internet gambling sites beyond the reach of the Federal Government. Without the authority previously provided by the Wire Act, there is no legal or regulatory framework for law enforcement to shut down illegal activity and millions of Americans will have no recourse if they become the victims of fraud or other criminal acts to seek redress. There is no enforcement mechanism to provide prompt and accurate payments, to prevent criminals from entering the marketplace, rigging games, taking advantage of children, or misusing customer identification and financial data.

The U.S. Department of State's 2012 International Narcotics Control Strategy Report (INCSR) stated:

> While not a major regional financial center, Costa Rica remains vulnerable to money laundering and other financial crimes, including various schemes that

target U.S.-based victims. Money laundering activities are primarily related to the foreign proceeds of international trafficking in cocaine. *A sizeable Internet gaming industry also launders millions of dollars in illicit proceeds through Costa Rica and offshore centers annually.*

The Costa Rican government reported that their nation is primarily used as a "bridge" to send money to and from jurisdictions and other offshore financial centers. The State Department noted several obstacles preventing the Costa Rican government from properly investigating and prosecuting money laundering offenses by not fully utilizing law enforcement tools like cooperating witnesses, confidential informants, electronic surveillance and undercover operations. In addition, money laundering cannot be charged as an additional offense to another crime in Costa Rica. You can prosecute and convict an individual for narcotics trafficking, but then they cannot also be charged with laundering the profits from the drug sales.

Organized criminals engaged in money laundering know that they can exploit these shortcomings in countries like Costa Rica, which is why they set up shop there. This is starkly demonstrated by the fact that 4 of the 11 individuals indicted by the U.S. Department of Justice for operating online gaming sites listed their residence as Costa Rica.

These 11 defendants were charged for violations of UIGEA and the Illegal Gambling Business Act (IGBA). The latter Federal statute was adopted by Congress in 1970 in an effort to attack the profits of organized crime. Apart from the individual making the wager, the statute allows any person that plays a role in the business or organization of conducting a gambling business to be charged with violating or conspiring to violate the Act. A key component to this law, however, is that there must be a *State* statute prohibiting the activity, which then would allow the Federal Government to investigate and prosecute the case.

The IGBA does provide law enforcement with some means to investigate organized money laundering based offshore. It also presents some questions about the reach of the law because the activation of the statute is dependent upon the state law. The indictments I mentioned earlier were brought using the State of New York, which defines gambling as taking place based on the location of the bettor. In other states, bettors may be able to call-in their wagers to an offshore bookmaker and not be in violation of state law, thus precluding the Federal Government from using the IGBA to go after these criminal enterprises.

Recent reports and investigations in Europe demonstrate that organized crime in Italy is laundering what one law enforcement official described as "enormous amounts of money" using online gaming sites in Germany. In 2007, the individual German states took over regulation of gambling, but there are no criminal penalties for using or operating an illegal gambling site. The illegal online gaming market is booming in Germany and criminal enterprises are taking advantage of it.

We know this for certain: organized crime is using offshore online operations to launder their profits. We also know that terrorist organizations are or could be using the same strategies to launder funds. According to counterterrorist analysts at Jane's Strategic Advisory Service, there are indications that terrorists in Afghanistan have been using illegal gaming sites to launder their money.

Illegal profits from unlawful activities are not of much use to criminal operations unless the money can be cleaned through legitimate channels. Without money laundering, organized crime could not exist. With changes in the how the Wire Act can be used, the limitations of both the UIGEA and IGBA, law enforcement in the United States does not have the means to effectively identify and shut down these operations.

The FOP is not advocating for any expansion in defining what online gaming activity is deemed unlawful. This was the position we took when we supported UIGEA and it is the position we still hold.

I believe U.S. law enforcement can rise to the challenge and successfully attack online fraud, money laundering and illegal gaming. Frankly, it is ridiculous that the Federal Government continues to regulate dynamic, ever-changing technology with legislation crafted in 1961. In 1961, we were dealing with the Bay of Pigs, the Beatles were first preforming and President Obama was born. Time certainly has marched forward and it is vital we address this issue before we fall even further behind. Continuing to wait on this issue will only cause it to become more serious.

We need Congress and the Administration to work with Federal, state and local law enforcement to devise an enforcement and regulator framework that will allow us to identify and go after organizations and businesses that are participating in or funding illegal activity. I am confident that we can do that if we work together.

I want to thank you again, Madam Chairman and Senator Heller, for the invitation to testify here today and I am ready to answer any questions you may have.

Senator MCCASKILL. Thank you, Mr. Canterbury.

We welcome Mr. Matt Smith from the Catholic Advocate. Thank you, Mr. Smith.

STATEMENT OF MATT SMITH, PRESIDENT, CATHOLIC ADVOCATE

Mr. SMITH. Thank you, Madam Chairman and Senators. Nearly 7 years ago, Congress voted overwhelmingly to protect vulnerable communities within our country, as well as the integrity of professional sports, by stopping the expansion of gambling on the Internet. Unfortunately, Congress' clear intent in the Unlawful Internet Gambling Act of 2006, UIGEA, is now under assault.

At the behest of two state lotteries 2 days before Christmas, as Senator Heller already stated, the Justice Department announced it was upending more than five decades of consistent interpretation of the Wire Act, which prohibited all gambling over the Internet, with a new unilateral opinion that the law simply applied to online sports gambling. The Department of Justice's floodgates, as Senator Heller also stated, have opened the floodgates for states to accelerate plans, many already underway, to go even beyond ticket sales to offer casino-like games on the Internet under the umbrella of their State lottery.

The CEO of the leading provider of lottery services in the United States was quoted saying, "The DOJ ruling does not limit the sale of authorized products solely to State lotteries. I think it's possible that if lotteries are B-to-market, they could be tarnished by the early entrance and also risk the ability to attract younger players." It is those younger players and other vulnerable populations, like seniors, who are most at risk. Ninety-three percent of teens aged 12 to 17 utilize the Internet, and 97 percent of teens of the same age participate in some form of online gaming, making them attractive targets for gambling marketing, as well as illegal and fraudulent operators.

By reinstating the more than 50-year interpretation of the Wire Act and strengthening UIGEA, you can protect our children and families from the erosion of safeguards Congress has previously established.

We recognize Congress did not create this problem, but here is an opportunity to address an impending matter before it becomes a crisis. Congress has the power to protect our seniors, our children, and give law enforcement the tools they need to protect the vulnerable from illegal predatory gambling interests. We urge bipartisan congressional action to restrict the imminent expansion of online gambling throughout states, lotteries, and offshore operators, and believe Federal restriction of online gambling is vital, urgent, and consistent with congressional intent.

Thank you.

[The prepared statement of Mr. Smith follows:]

PREPARED STATEMENT OF MATT SMITH, PRESIDENT, CATHOLIC ADVOCATE

Nearly seven years ago, Congress voted overwhelmingly to protect vulnerable communities within our country as well as the integrity of professional sports by stopping the expansion of gambling on the Internet. Unfortunately Congress' clear intent in the Unlawful Internet Gambling Act of 2006 (UIGEA) is now under assault.

A pro-Internet gambling coalition of large states desperate for more revenue and foreign-owned gambling companies have lobbied the Executive Branch to get around Congress' intended protections and, at the end of 2011, they received an extraordinary boost from an unlikely source: the U.S. Department of Justice. On Friday, December 23, 2011, the Justice Department (DOJ) announced it was upending more than five decades of consistent interpretation of the 1961 Wire Act which prohibited all gambling over the Internet with a new, unilateral opinion that the law simply applied to online sports gambling.

The *Wall Street Journal* described what happened next: "When the U.S. Justice Department in December narrowed its interpretation of the 50-year-old Wire Act, saying it banned only sports betting and not other forms of online gambling, the decision sparked hope in state capitals that lotteries could start selling tickets online and lead a charge into online gambling." The "charge into online gambling" was exactly what Congress intended to prevent—with very good reason.

DOJ's determination has opened the flood gates for states to accelerate plans, many already underway, to go even beyond ticket sales to offer casino-like games on the Internet under the umbrella of their state lottery system. Several states have either passed online gambling statutes or are in the process of passing them quickly in upcoming sessions to take advantage of the Department of Justice ruling.

The CEO of the leading provider of lottery services in the United States has said, "The DOJ ruling does not limit the sale of authorized products solely to state lotteries. I think it's possible that if lotteries are beat to market, they could be tarnished by the early entrants and also risk losing the ability to attract younger players."

It's those "younger players" and other vulnerable populations like seniors who are at the most serious risk. Ninety-three percent (93 percent) of teens age 12–17 utilize the Internet and 97 percent of teens of the same age participate in some form of online gaming making them attractive targets for gambling marketing as well as illegal and fraudulent operators.

Often, Congress is put in situations where issues that are already problems require solutions. Here is an opportunity to address an impending matter before it becomes a crisis. Congress still can act to reassert its authority and re-establish its intent to prevent the proliferation of online gambling in the U.S. By reinstating the more than 50-year old interpretation of the Wire Act and actually strengthening UIGEA, you can protect our children and families from the erosion of safeguards Congress has previously established.

We recognize Congress did not create this problem. Congress, though, does have the power to protect our seniors, our children, and give law enforcement the tools they need to protect the vulnerable from illegal predatory gambling interests. We urge bi-partisan congressional action to restrict the imminent expansion of online gambling throughout states, lotteries, and off-shore operators. Federal restriction of online gambling is vital, urgent, and consistent with recent congressional intent.

Senator MCCASKILL. Thank you, Mr. Smith.

We will now hear from Mr. Blum. Thank you very much for being here.

STATEMENT OF JACK A. BLUM, ESQ.

Mr. BLUM. Thank you, Senator. My name is Jack Blum. I am a Washington, D.C. attorney, and I specialize in money laundering compliance, offshore tax evasion, and financial crime. I am here this morning at the request of the Committee. I have no client interest at all in the gambling business. I think gambling is dumb, I do not do it, and so much for that.

Gambling and organized crime have quite a history, and I think it is worth spending a minute on that history because it is the origin of the Wire Act, and it is the heart of one of the big problems we are facing.

Al Capone got caught for income tax evasion, and Meyer Lansky was a man who solved the problem for organized crime way back when. And his idea was to own a racetrack, and use the racetrack as a way of legitimizing the take from organized crime. He got the Batista regime in Cuba to give him control of the racetracks, and

all of the organized crime money from the East Coast went into banks in Florida, essentially as winnings from the Cuban tracks. I saw the same thing go on again in the Caribbean when I worked on the island of St. Maarten, and I saw planeloads of cash coming into the airport in St. Maarten going into the bank, being deposited by an Italian Mafioso, who then controlled all of the casinos on the island. His idea was this is winnings from the casino, and, of course, if you went into the casinos, there were no customers there. But that was not why the casinos existed.

So, the question of who owns a casino is pivotal, and that is why casinos have to be licensed, and that is why states, like Nevada, New Jersey, who have brick and mortar casinos, go through a very vigorous and rigorous process of licensing casino owners. Now, I think that the problem of going on the Internet has made the issue of licensing even more important. Who is it that has this Internet casino? Is it someone legitimate? And here, the problem is they can operate from anywhere, and I really cannot fathom how any states can control something that operates that way from anywhere in any jurisdiction.

The offshore casinos have figured out how to evade U.S. law. They have been doing it for a long time. If you want to take a look at it, all you have to do is go on the web and do a search. And now on top of everything else, we have an artificial currency called "BitCoin," which could even take it out of the realm of being able to police it through the banking system.

I began to look into one aspect of this for part of the Federal Government, which is the offshore merchant business, and we were trying to figure out how people were using offshore accounts to evade taxes. We discovered that there were service companies in places like Bermuda and elsewhere that were offering completely set up online casinos to people, and these casinos were part of what were called, "protected shell corporations." The protected shell corporations had no visible owners. If you went to Bermuda, all you could find would be the parent company of the protected shell, which actually had the bank account, and there would be no way of getting to the person who really owned the casino. That is, from a regulatory point of view, a complete nightmare.

In truth, the casino is a bank. Any business organization that has an encrypted switch and can take open accounts, take money, and send money, is operating as a bank. And as a bank, it comes under the Bank Secrecy Act and all of the rules regarding money laundering.

So the question is, how do you now regulate these online casinos in any meaningful way, and how do you apply the Bank Secrecy Act to it? We are currently having a huge problem with our regular banks, getting them to comply with money laundering laws. I am sure you have all seen the accounts of HSBC, a major international bank, laundering $4 trillion. If the Treasury Department is having a problem with HSBC, how is it going to handle the Internet gaming industry, which is sprawling and global?

Up until now, it has been the banking industry which has controlled the offshore gaming industry. And the way that worked was the prohibitions of the Uniform Act, which said banks really were the ones who were responsible for preventing the opening of ac-

counts without knowing your customer, without being sure that the customer was legitimate. Now that that Act has been undermined, the banks are wide open to accept these customers without the kinds of money laundering controls that previously existed.

My belief is the only way we can get on top of this is to have a regulatory agency at the Federal level that licenses online casinos where casinos are prohibited—foreign casinos are prohibited from operating in the U.S., and any U.S. player who uses one is subject to penalty. And that way, we might possibly be able to both tax and control the bad behavior of the people who want to use casinos to launder money.

My special concern is that some of this casino operation could be used to move funds from the United States to a foreign destination. Gambler in the U.S. sets up an account, puts money in the account. The unscrupulous casino operator sends the money to another account in an offshore location. Likewise the money could be moved back exactly the same way.

We really have to have comprehensive Federal regulation, sophisticated Federal regulation, and it should happen sooner rather than later because, as I say in my prepared testimony, the cat is out of the bag.

Thank you.

[The prepared statement of Mr. Blum follows:]

PREPARED STATEMENT OF JACK A. BLUM, ESQ.

My name is Jack A. Blum. I am a Washington, D.C. lawyer specializing in money laundering compliance, offshore tax evasion and financial crime. I am appearing here this morning at the request of the Committee. I do not have clients with an interest in Internet gambling. Personally, I think gambling is dumb and I learned early on that the house always wins.

Gambling and organized crime have had a long standing relationship. When the Justice Department nailed Al Capone it was for tax evasion. The financial wizard of organized crime, Meyer Lansky, understood that criminal proceeds had to be legitimized. He taught the criminal world that the best way to do it was to own either a race track or a gambling casino. Lansky gained control of Cuba's race tracks before the outbreak of World War II. The East Coast's organized crime families deposited their profits from prostitution, illegal gambling, and drugs in the Cuban race track's bank accounts in Florida as the track's take on the pari-mutuel betting in Cuba. Magically, criminal proceeds from the U.S. East Coast became legitmate race track profits from Havana.

In the early 1990s I was hired to investigate money laundering on the Caribbean island of St. Maarten. An Italian with organized crime connections had taken over the island casino business. Each day the casinos deposited large amounts of cash as the "house take." In fact when I visited the casinos there were very few customers and hardly enough activity to bother keeping the doors open. I found the explanation at the St. Maarten airport where each day flights would arrive from San Juan and Miami and would be met by armored cars. Mailbags of cash were offloaded and taken to the banks to be deposited as gambling winnings. The Dutch Ministry of Justice and the DEA broke the mafia hold on the island and the laundering stopped—at least for a while.

The moral of these stories is simple—casino ownership and operation must be regulated. Casino books need to be audited and the gaming should be supervised to prevent buying and selling chips from becoming another way of laundering cash and to prevent the casino being used to cover large criminal money movements. The states that got into the business early, Nevada and New Jersey learned their regulatory lessons the hard way and established respected regulatory organizations. Other states followed suit and as long a gambling was tied to bricks and mortar the problems were manageable.

Unfortunately, the development of the Internet and global electronic commerce has made serious control of gambling very difficult. In the new world of electronic commerce the definition of a financial institution has become any business enter-

prise that has an encrypted switch—that is to say it has customer accounts from which funds come and go and which are protected through some form of encryption. Functionally an online casino is no different than a bank even though its purpose is different. It has customer accounts that have balances. Customers can add or withdraw money at will, and if the operator is willing, balances can be transferred from one account to another. It stands to reason that a casino should have the same anti-money laundering controls that banks have. Casinos should be required to know their customers, they should be required to monitor accounts for suspicious transactions, and casinos should be audited for the protection of customers and to insure compliance with the anti-money laundering regime.

Online casinos can operate from any jurisdiction. Offshore casinos have developed sophisticated methods of avoiding supervision and U.S. law. I suspect more than a few of the existing offshore casinos have money laundering and illicit funds transfer as their principal purpose.

To make matters worse we now must confront the use of artificial currency such as the Bitcoin that is beyond the reach of governments.

As part of a consulting assignment for a Federal agency I began to look into what is called the offshore merchant business. The idea behind becoming an offshore merchant was that a business based on the Internet could direct all customer payments for services in the U.S. to an offshore account that would accept credit cards. The funds would be untraceable and the offshore merchant would thus avoid showing income in the U.S. and evade Federal and state tax.

To make the offshore operation opaque service providers in offshore jurisdictions offered "cells" in what are called protected cell companies. These companies have an overarching company with bank accounts and a visible identity, but they are made up of individual cells, each with a different owner, and each financially independent of the other. There is no way for foreign law enforcement to find the ownership of the individual cell companies. Even the local governments do not know the owners of the cells.

Protected cells are just one of a number of ways of hiding financial operations offshore. Untraceable shell companies, trusts and other devices are in widespread use. Indeed, Senator Levin has introduced legislation aimed at putting an end to anonymous corporations here in the U.S.—legislation that I strongly support.

In doing my research, I found several service providers who offered casino gambling site software with a full complement of games and the ability to set up individual customer accounts. By the way—many of these same service providers also offered pornographic sites protected by a pay firewall. The software is designed to be controlled by an individual cell company far out of reach of regulation, taxation, and prosecution for fraud.

Congressional efforts at controlling offshore online gambling activities have met with limited success. The principal piece of legislation in this area is the 2006 Unlawful Internet Gambling Enforcement Act. That Act bars the use of checks and credit cards in payment for illegal gambling activities. The word is "illegal." The definition of illegal was based on the Wire Act of 1961 that banned the use of interstate wire communications for both sports and no-sports gambling. The ban on the use of payment systems put the banks in the business of policing customers to make sure the only online firms that used bank accounts and credit cards were offering "legal" gambling services—that is to say gambling allowed by state law.

The one prosecution and conviction of note under the UIGEA targeted the operators of a sports book based in Antigua that accepted bets from U.S. persons. The operators of the sports book, Daniel Eremian and Todd Lyons, operated openly and flamboyantly, almost daring the Department of Justice to prosecute. Most likely at their instigation the government of Antigua filed a complaint against the United States under the WTO rules. Antigua claimed that the U.S. law aimed at their offshore casinos was an act of trade discrimination.

As the prosecution of Sports Offshore was taking place, the Department of Justice changed its interpretation of the Wire Act. It said that the Act only applied to sports betting. The Justice opinion ended the effectiveness of the ban on bank transfers and credit cards for casinos that limited themselves to electronic table games and slots and left the field wide open for gambling websites. After the DOJ opinion, websites that offered casino games that were now considered legal could use bank payment systems.

To the extent that the controls on payments for online gambling worked, they kept American customers away from the offshore sites. The Justice Department decision to give up on the control of interstate gambling other that sports gambling has opened the door wide to any entrepreneur legitimate or otherwise who wants to get in the business. It tore up the Wire Act—an Act that was the result of extensive hearings on organized crime and gambling by Senator Estes Kefauver and the

Senate Permanent Investigations Subcommittee. It left behind a maze of state laws and no real way of regulating the Internet gambling business.

The current situation raises the question of whether there will be any controls on the business of Internet gambling or whether we will go back to the days of Al Capone and Meyer Lansky. To prevent money laundering through an Internet site the sites will have to be licensed, audited, and regulated. The applicants for a license will have to be screened for fitness and to ensure they do not have criminal pasts or criminal connections. The operations will have to be audited to insure that the stated earnings in fact come from "house" winnings. Customers will have to be subjected to due diligence under 'know your customer' rules. Casino operators will have to file suspicious activity reports on customer accounts with the Treasury's FINCEN. They will have to be audited to insure the suspicious activity reports are in fact filed and that the operators are screening customers and the activity in customer accounts.

There will also have to be systems to insure that winnings are reported to IRS and taxes are paid.

Finally, the auditors will have to insure that the online casinos do not become sophisticated money transfer systems—a kind of online Hawala exchange. An unscrupulous operator could take funds from a U.S. gambler, and pay "winnings" to a foreign player's account. Or the money could move from an offshore player to an onshore player. The possibilities for terrorist financing and for moving the proceeds of white collar crime using this system are endless.

What part of government will take on the regulatory responsibility? What part of the government is equipped to supervise a sophisticated and very large financial industry? Most certainly it cannot be the IRS—an agency that has had its budget cut three times in the past three years and has been given the added responsibility of implementing the new healthcare legislation. You will have to create a new specialized regulatory agency, perhaps as a part of the Treasury Department that will take on the job.

The regulatory problem cannot be solved by a software system alone no matter how sophisticated the system is. Screening systems all require human intervention to screen the computer search results and to integrate the results in ways that lead to enforcement action. Moreover we have all seen what happens when a financial institution, which a casino is, gives up on its regulatory responsibility. The example I have in mind is HSBC which laundered four trillion dollars in drug money, computer screening systems notwithstanding.

I believe that the new regulatory agency Congress will have to create will have to be staffed by experts with the resources to do the hard work of keeping the industry honest. I do not think this kind of regulation can be done at the state level. The regulation will be expensive and the industry will have to be taxed to pay for regulation.

I do not believe prohibiting Internet gambling will work. The horse has left the barn. The Internet is too open to control and in any event controls will not work across state and national borders. What we have to hope is that a new Federal agency can inspire enough trust to encourage customers to use U.S. sites, and that competitors will report problem sites to the regulators and the law enforcement authorities. The regulators will also have to screen the Internet regularly for pop-up casino sites that are attempting to avoid controls. There will have to be limits placed on bank transfers to offshore casinos.

You will have to address the issue of online gambling one way or another. The sooner the problem is addressed the better because the present situation is out of control. A simple Internet search for online casinos will show you how many players have entered the field. Crafting appropriate legislation will take a concerted effort by Congress with the help of the agencies now tasked with money laundering prevention.

I hope you have found this testimony helpful and I will be happy to answer any questions you may have.

Senator MCCASKILL. Thank you, Mr. Blum. And all of your statements will be included in the record.

Mr. BLUM. Thank you.

Senator MCCASKILL. Mr. Grissen?

STATEMENT OF THOMAS A. GRISSEN, CHIEF EXECUTIVE OFFICER, DAON

Mr. GRISSEN. Thank you, Madam Chair, Ranking Member Heller, and other members of the Subcommittee. I appreciate the opportunity to testify and discuss some of the topics in front of this committee. You have my written testimony. I hope you find today's demonstration valuable. I appreciate your insight to see the new innovative technologies.

I will just take a few seconds to make three points prior to proceeding with the demonstration. The first point is that I am not a proponent or an opponent to Internet gaming. My focus is on technology and establishing trust on the Internet and those people that interact online. I do share your concerns about the developments that are occurring in the states.

The second point would be that there is a much broader consumer protection concern that spans all industries, not just Internet gambling. You may have seen today's *USA Today*. Colleges are struggling with online courses to make sure that the person enrolled and that is doing the homework, is the same person who takes the exam, so the concerns are widespread.

And this all comes back down to establishing a means of trust, so how do we know that the person we are interacting with are who they claim to be, and how do I protect and assert my identity?

Other industries are moving forward. Probably one of the first adopters of the technology would be banking. Their concerns are both in terms of differentiating the brand, but also security fraud and regulatory compliance. These industries are adopting new technologies, including biometrics, and biometrics are just factors that are uniquely you. Your voice would be different than my voice. Your face would be different than my face. Your fingerprint would be different than mine. So there are human characteristics that are uniquely you.

We all know that passwords are inadequate to serve these concerns. These comments, and the inadequacy of passwords have been expressed by everybody, including the President of the United States. We need to move forward to new technologies.

And with that, I would like to proceed with my demonstration. [See Exhibit B on pages 45 and 46].

For the demonstration, I am just going to use a standard Apple device, and on the device is a series of applications. The application I am going to choose is a banking application, but it could be anything. The menu presents me with options. In this case, I am going to select a second option, which is a transfer of funds.

I will transfer funds between a savings account and a checking account, and I am going to choose to transfer a substantial portion of funds. Let us say I am going to transfer $15,000 to my son for his college tuition, so I select "transfer." It is asking me to confirm that transaction. I choose to confirm the transaction, and the system, based on the policy, is asking me first for a PIN, so I enter my PIN. It is now saying that the transaction is of some consequence to me, and what I would like to do is verify that you really are who you claim to be as opposed to just something I know.

It is asking me to take a photograph, which I will do. There could be jokes about that. I am sorry you are laughing at my imagery,

but I am submitting the photograph. And again, because of the considerations of the sum of monies involved, it is asking me to speak a phrase. I am going to speak this phrase. My identity is secure because my voice is my passport. Verify me.

And what it is doing is taking all those identity attributes, it is encrypting them, it is sending them off to the server, it is matching them against an enrollment record, it is verifying mathematically that it is me in each of those attributes. My face, my voice, the PIN, the crypto keys on the phone match the enrolled identity. It is confirming the transaction, and it is establishing online trust. That would be the consumer experience. These are the technologies being rolled out by banks as we speak. And you will see them adopted in other industries.

Now there is another important role associated with this technology, and that is of a regulator or an operator. I am going to select a different application, and this would be a command center. So this would be the back-end technology.

"My identity is secure because my voice is my passport. Verify me."

That would be the verification I just went through. And so, you would have a forensic audit trail of each and every transaction. And on the top half of your screen, you see a variety of transfers for each transaction or identity event I ever undertook. I would be able to verify the biometrics associated with those identity events, including my face, my voice. And I would also be able to see other information on the transaction, including the location of the transaction and where it occurred. In this case, for the back-end operator, to save time in this hearing, this transaction was performed earlier this week and we just took the screen images of it, so that actually did not go into the back end of the system.

The design of the system is to take a tool that consumers have, love, use, very convenient, and couple that with powerful technologies designed to establish trust between an identity event online and the individual doing it, and then to use the back-end command center allowing a regulator to investigate any transaction they wanted.

Thank you very much.

[The prepared statement of Mr. Grissen follows:]

PREPARED STATEMENT OF TOM GRISSEN, CHIEF EXECUTIVE OFFICER, DAON

Thank you, Chair McCaskill, Ranking Member Heller, and members of the Subcommittee, for giving me the opportunity to testify today on this important topic. My name is Tom Grissen and I am the CEO of Daon, a leading provider of identity assurance, identification and verification software services worldwide. Our customers include the Departments of Commerce and Homeland Security, two of the largest American banks and many other large, private corporations, most of our Nation's airports and maritime ports, the EU, Japan, Australia and many other countries around the world.

I will argue that the tools we have been relying on to address cyber security are inadequate. I hope to persuade you that there is a new kind of solution that will fix the broken trust model of the Internet. As we speak, these technologies are being deployed across some of the most sophisticated financial institutions in the world.

Over the next five minutes of my testimony a drama will be playing out across the Internet. Hundreds of millions of Internet transactions will occur touching nearly every aspect of one's life.

We will demonstrate the relevance of new technology through obvious applications in banking. At the same time the technology can be applied in ways that one can

scarcely imagine across industries such as health care, social networking and online gaming.

The crux of the problem across all these industries is that we cannot effectively identify the individuals with whom we interact online.

We have all enjoyed the eye opening experiences of the Internet. We all went online to *browse* websites and found innovative companies such as Netscape. Then we found the wonderful advancements in *search* and benefited from great companies such as *Google.* Next we placed our digital lifestyle on the Internet through companies such as *Facebook* who tapped into our desire to SHARE. What is missing is an effective means of establishing online *trust.* Technologies similar to what you will see today address this daunting problem.

The inadequacy of the tools to establish online trust is understood by everyone, including the President of the United States. In the current online environment, individuals are asked to maintain dozens of different usernames and passwords, one for each website with which they interact. Passwords have served us well, but were invented in the 1960s. The complexity of this approach is a burden to individuals and encourages bad behavior—like the reuse of passwords—that makes online fraud and identity theft easier. Challenge response technologies are being defeated by social engineering. They all depend on "what someone knows" rather than "who you are."

Daon develops software that binds the person to the event through the use of factors, including biometrics. Biometrics are simply human characteristics that are uniquely you, such as your voice, face, palm, fingerprint, etc.

Using your smart phones, PCs or tablets, these software technologies empower you to securely establish your identity through a combination of encryption, PIN/passphrase entry, location-based technology, and biometrics such as voice, face and palm image matching. These technologies are a fully mobile, private and cost effective solution based on technology (*e.g.,* smart phones) that consumer's use and enjoy.

I am neither a proponent nor an opponent of Internet gambling. However, there are many parallels between Internet gambling and what Daon does for our clients in terms of the trust relationships with customers and the governmental oversight of various activities (*e.g.,* financial services). Over the past two years we have been monitoring the development of this issue before Congress. Absent congressional action or a uniform set of national standards for this particular Internet activity, various states have authorized various forms of Internet gambling. We have watched as states such as Illinois, Nevada, New Jersey and Delaware have either rolled out or are preparing to roll out Internet gambling with different kinds of standards for age verification, location verification and fraud prevention.

I am thoroughly convinced, particularly in the wake of the December 2011 Justice Department decision about the inapplicability of the Federal Wire Act to most forms of Internet gambling, that continued congressional inaction on this issue is not acceptable.

The risks associated with Internet gambling—and in particular, Internet gambling that is either unregulated or insufficiently regulated—are well-appreciated. These include:

- Gambling by minors;
- Defrauding of consumers by site operators;
- Defrauding of players by other players;
- Money laundering by either operators or players;
- Violations of jurisdictional restrictions or prohibitions;
- Breaches of data confidentiality and other security failures; and,
- Problem or excessive gambling.

Despite the recent indictments of several prominent offshore poker operators, no one can seriously challenge the fact that Americans, young and old, are finding ways to gamble on illegal offshore sites—some estimates put the markets at several billion dollars. But illegal offshore sites are only part of the problem, as the states, in the wake of the DOJ decision, are pursuing their own Internet gambling ventures. For example, the Illinois Lottery has been selling tickets online since March 2012. Georgia has sold lottery tickets online since November 2012. Legal online poker has taken place in Nevada since April 2013. Delaware has approved Internet casino-style gambling and its system is expected to be operational by October. My understanding is that Internet gambling of all kinds will go live in New Jersey this November.

There are many other states weighing proposals of one kind or another to legalize Internet gambling (See Exhibit A for a discussion of Internet gambling legalization

across the U.S.). While all of these states have some standards to deal with identifying customers and other regulatory issues, both the existing Internet gambling states and the prospective Internet gambling states share one common attribute: in no jurisdiction is state-of-the-art "Know Your Customer" technology in place or required to adequately mitigate the risks of Internet gambling. In other words, no one has technological requirements in place to ensure that a minor is not playing on a stolen parent's credit card and PIN; that it's a human being you're playing against, not a robot; or that a player is actually physically located in a jurisdiction that permits Internet gambling.

Satisfying these requirements means employing systems already in place for many sensitive e-commerce and security applications. Exhibit B provides screen shots demonstrating how the systems work.

As the Internet by its very nature transcends intrastate commerce and is truly interstate, establishing our nation's policies on Internet gambling is the responsibility of the Congress. Whether the policy is prohibition, limitations or some combination, is your choice. But, given the current proliferation in the states, I believe that one appropriate role for the Congress—and I believe the time is ripe for Congress to exercise this role—would be to set certain strict, minimum standards for identity assurance, identification, and verification for Internet gambling should the states be permitted to offer it in the first place. Nothing in the track record thus far suggests that states will apply such standards of their own volition, and it's time Congress stepped up to the plate.

Thank you again for the opportunity to testify and I look forward to your questions.

GamblingCompliance

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WHAT'S NEW IN THIS EDITION?

Introduction: The Federal and State sections have been updated.

U.S. Internet Gambling Regulatory Map: The map has been updated.

Delaware: The Timeline section has been updated.

Nevada: The Current Status and Timeline sections have been updated.

New Jersey: The Current Status and Timeline sections have been updated.

California: The Current Status and Timeline sections have been updated.

Pennsylvania: The Timeline section has been updated.

Federal: A new section has been added.

Dead Legislation: Texas has been added.

U.S. Internet Gambling Legislation Monitor: The monitor has been updated.

U.S. Internet Gambling Reference Table: The table has been updated.

U.S. Internet Lottery Ticket Sales Monitor: The monitor has been updated.

NOTABLE DATA

No. of states that have considered Internet gambling legislation

10

2013 (State)

No of states that considered Internet gambling legislation

9

2012 (State)

Total amount spent ($m) lobbying Internet gambling legislation

30.5

112th Congress (Federal)

INTRODUCTION

Federal

Internet gambling legislation was introduced in the House on June 7.

The bill, sponsored by Democratic Rep. Peter King of New York, would create an interstate Internet gambling regulatory program overseen by the Treasury Department in conjunction with qualified state and tribal regulatory bodies.

King, who chairs the House Homeland Security Committee, is a long-standing Internet gambling proponent. He co-sponsored the first-ever bill to legalize the activity in 2007 alongside former Democratic Rep. Barney Frank of Massachusetts.

Lobbyists told GamblingCompliance the King bill is not expected to move. They said it is intended chiefly as a "marker" to keep Internet gambling on the congressional radar.

Meanwhile, Democratic Senate Majority Leader Harry Reid of Nevada, whose recent pushes to legalize Internet poker have fizzled, told the Las Vegas Sun in early June that getting a bill passed this session will be difficult. "I felt for several months now that I don't see any movement on this," Reid said. "I don't see anything happening."

A purported draft bill from Reid's office last year, which would have authorized Internet poker but tightened restrictions on other forms of gambling, was opposed by Indian tribes and state lotteries. If taken up again this year, the draft bill is expected to draw further opposition from those groups.

In the first quarter of 2013, federal Internet gambling lobbying spend plummeted 40 percent to $2.3m, down 40 percent compared to the fourth quarter of 2012.

State

Internet gambling legislation is pending in California, Massachusetts and Pennsylvania.

In Texas, Internet poker legislation has died, making the state the fifth behind Hawaii, Illinois, Iowa and Mississippi to scupper a legalization bid this year.

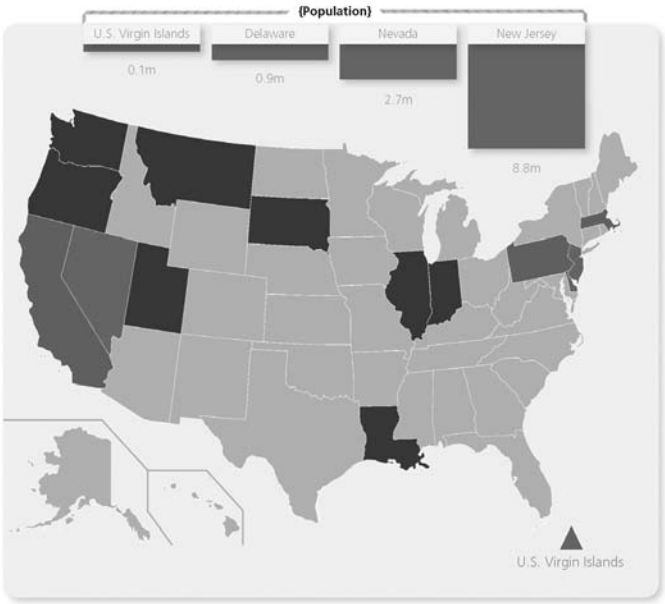
In California, a coalition of influential tribes floated draft Internet poker legislation in early June. The proposal is backed mainly by the San Manuel Band of Mission Indians. A separate draft proposal, floated by the Pechanga Band of Luiseño Indians in conjunction with other, large gaming tribes, is also in play. The two tribal groups are in the process of negotiating compromise language. If agreed, the language could debut later this year, tribal lobbyists told GamblingCompliance in late May.

In Michigan, Internet lottery remains in limbo. Provisions to fund the move have been stricken from the Legislature's proposed budget. But so too have provisions that would effectively prohibit the lottery from expanding online. The lottery in mid March closed an "iLottery" RFP but has yet to name a winning bidder. The lottery is in the process of negotiating a move-forward solution with the Legislature, its spokesperson told GamblingCompliance in early June.

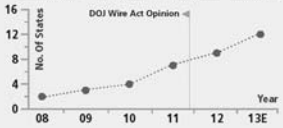
In New Jersey, regulators are preparing to launch Internet gambling. Draft rules were published in mid May. And in late May, Mario Galea, the former head of Malta's Lotteries and Gaming Authority, was retained to assist with the roll out. Operations are expected to commence on or before Nov. 26, 2013.

Internet poker is live in Nevada and Internet gambling is expected to go live in Delaware on or before Sept. 30, 2013.

U.S. INTERNET GAMBLING REGULATORY MAP: JUNE 2013



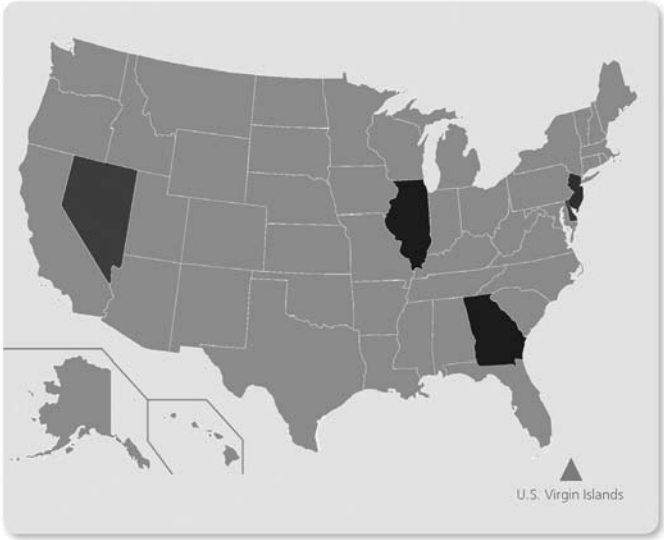
No. Of States Considering Bills



Key

- Internet gambling regulated
- Internet gambling legislation pending
- Internet gambling expressly prohibited

U.S. INTERNET GAMBLING COMMERCIAL ACTIVITY MAP: JUNE 2013



Key

- Regulated: Poker
- Regulated: Poker, Casino or Bingo, and Lottery
- Regulated: Lottery
- Regulated: Games TBD
- Regulated: Poker and Casino or Bingo

DELAWARE {REGULATED}

Overview

Delaware is considered one of the smallest prospective Internet gambling markets in the United States given its population, approximately 907,000 residents, is among the lowest in the nation. An exact valuation of the market, however, has not been made public by private or governmental sources.

Current Status

An Internet gambling bill, **HB333** (at right), was enacted in June 2012. It authorizes the Delaware Lottery to offer and administer an Internet lottery. Internet table games and video lottery games will be offered via a website or websites branded and promoted by the state's three racetrack casinos, sharing one technology platform. Sale of Internet ticket games, meanwhile, will be conducted by the Delaware Lottery Office. However, players must purchase prepaid cards or a similar mechanism from a retail lottery agent to purchase Internet ticket games. That restriction does not apply to table games or video lottery games. The law also authorizes expansion of keno and the Delaware Sports Lottery at licensed retail establishments and provides cuts for racetrack fees. For now, the law only allows intrastate Internet gambling, but it provides that interstate gambling may occur in the future.

Timeline

In early May, the lottery named Scientific Games and partners WMS Industries and 888 Holdings as its primary Internet gambling vendor. Additional game-content and support-services vendors are expected to be named soon. Internet bingo, keno, video lottery games and casino table games are expected to launch no later than Sept. 30. Internet poker will not launch until the lottery has a liquidity-sharing agreement in place with another state. Draft Internet gambling regulations, meanwhile, will be published before the September go-live deadline.

Quick Facts

Gaming Activity Allowed	
Internet Poker	✓
Internet Casino or Bingo	✓
Internet Lottery	✓
Regulation	
Intrastate	✓
Interstate	✓
Operator Licensing	
Monopoly	✓
Land-Based Incumbents	
Open	
Supplier Licensing	
Non-Restricted	✓
Restricted	
Regulator	
Lottery	✓
Age Requirements	
18 Years or Older (Lottery)	✓
21 Years or Older (Other)	✓
Advertising Permitted	
Yes	✓
No	
Tax Rates	
33.9% Table Game Proceeds	✓
56.5% Video Lottery Proceeds	✓
Lottery Proceeds (Tax-Exempt)	✓

NEVADA {REGULATED}

Overview

Nevada is considered one of the smallest prospective Internet gambling markets in the United States given its population, approximately 2.6m residents, is among the lowest in the nation. A January 2011 study conducted by Applied Analysis, an independent economic consultancy, estimated that Internet poker alone could generate between $2m and $3.3m, annually, in state-governmental tax receipts.

Current Status

Interactive gaming is legal in Nevada. **Regulations** governing the offering of interactive gaming (at right) were implemented in December 2011. Additional regulations were implemented this year. Under them, operator licensure is open exclusively to Nevada-based terrestrial gaming operators. Supplier licensure, by contrast, is not exclusive to such operators.
State law formerly prohibited interactive gaming from commencing without prior authorization from Congress or the U.S. Justice Department. But on Feb. 21, 2013, a bill, **AB114** (A, at right), was enacted that allows interactive gaming to commence without such authorization. Additionally, it permits the governor to execute interactive gaming agreements with other states. The bill also prohibits Internet gambling businesses that knowingly and intentionally took or facilitated U.S. bets after Dec. 31, 2006, from obtaining interactive gaming licensure for five years. On June 11, 2013, **AB360**, which, among other things, authorizes the governor to execute interactive gaming agreements with foreign governments, took effect.

Timeline

Interactive gaming went live on April 30. That day, Ultimate Poker, a subsidiary of Station Casinos, dealt the country's first hand of regulated, real-money Internet poker. Other operators are expected to launch in the coming months. Republican Gov. Brian Sandoval, meanwhile, has held preliminary talks with other states about interactive gaming agreements.

Quick Facts

Gaming Activity Allowed	
Internet Poker	✓
Internet Casino or Bingo	
Internet Lottery	
Regulation	
Intrastate	✓
(A) Interstate	✓
Operator Licensing	
Monopoly	
Land-Based Incumbents	✓
Open	
Supplier Licensing	
Non-Restricted	
(A) Restricted	✓
Regulators	
Gaming Commission	✓
Gaming Control Board	✓
Age Requirement	
18 Years or Older	
21 Years or Older	✓
Advertising Permitted	
Yes	✓
No	
Tax Rate	
6.75% of GGR	✓

NEW JERSEY {REGULATED}

Overview

New Jersey is considered one of the largest prospective Internet gambling markets in the United States. To date, it also the most populous state to legalize Internet gambling. An exact valuation of the market remains elusive, however. In late February, Republican Gov. Chris Christie modeled $180m in Internet gambling tax revenue into his proposed FY 2014 budget. However, in late December 2012, the state Office of Legislative Services declined to offer a tax-revenue estimate, citing "a lack of data."

Current Status

An Internet gambling bill, **A2578**, was approved on Feb. 26, 2013. **P.L. 2013, c. 27** (at right), authorizes Atlantic City casinos or their affiliates to apply for licenses to operate gambling websites. Internet gamblng revenue is effectively taxed at 17.5 percent or 20 percent. Internet gambling businesses that previously took or facilitated U.S. bets are allowed to apply for supplier licensure. The new law permits casinos to accept bets from players in other states and countries so long as such bets comply both with federal law and with the laws where players are located. The law will sunset after 10 years the state legislature does not re-authorize it. The Division of Gaming Enforcement published draft Internet gambling **regulations** on June 3. The regulations, among other things, outline proposed licensure requirements. The regulations are subject to a public comment period that will close on August 2. The comments will then be reviewed before final rules are adopted.

Timeline

The new law requires regulators to set a go-live date that is on or before Nov. 26, 2013. The go-live date will be announced at least 45 days prior to commencement. In order to participate in Internet gambling on the go-live date, interested suppliers must submit their license applications to the Division of Gaming Enforcement by July 29.

Quick Facts

Gaming Activity Allowed	
Internet Poker	✓
Internet Casino or Bingo	✓
Internet Lottery	
Regulation	
Intrastate	✓
Interstate	✓
Operator Licensing	
Monopoly	
Land-Based Incumbents	✓
Open	
Supplier Licensing	
Non-Restricted	✓
Restricted	
Regulator	
Div. of Gaming Enforcement	✓
Casino Control Commission	✓
Age Requirements	
18 Years or Older	
21 Years or Older	✓
Advertising Permitted	
Yes	✓
No	
Tax Rate	
17.5% or 20% of GGR	✓

U.S. VIRGIN ISLANDS {REGULATED}

Overview

The U.S. Virgin Islands is considered one of the smallest prospective Internet gambling markets in the United States given its population, approximately 109,000 residents, is among the lowest in the nation. An exact valuation of the market, however, has not been made public by private or governmental sources.

Current Status

Internet gambling is legal on the U.S. Virgin Islands. **Regulations** (at right) governing the offering of Internet gambling were implemented in November 2002. They authorize Internet gambling operators to offer Internet gambling both on the U.S. Virgin Islands and in other jurisdictions where the offering of such gambling is not prohibited. The U.S. Virgin Islands Casino Control Commission, however, has yet to prescribe which forms of Internet gambling are expressly permitted.

Timeline

The Casino Control Commission is not accepting license applications for Internet gambling and has not announced a timeline for when it will begin doing so. But in late January 2013, the Commission met with outside consultants and legal experts to discuss options for expanded gambling, including Internet gambling. Violet Anne Golden, a member of the Commission, said then that an Internet gambling licensing regime would be installed "sooner rather than later."

Quick Facts

Gaming Activity Allowed	
Internet Poker (TBD)	
Internet Casino or Bingo (TBD)	
Internet Lottery (TBD)	
Regulation	
Intrastate	✓
Interstate	✓
Operator Licensing	
Monopoly	
Land-Based Incumbents	
Open	✓
Supplier Licensing	
Non-Restricted	✓
Restricted	
Regulator	
Casino Control Commission	✓
Age Requirement	
18 Years or Older	
21 Years or Older	✓
Advertising Permitted	
Yes	✓
No	
Tax Rate	
1.5% of GGR	✓

CALIFORNIA {PENDING}

Overview

California is considered the largest prospective Internet gambling market in the United States. A 2010 study conducted by LECG, an independent economic consultancy, estimated that Internet poker alone could generate between $2.4bn and $6.1bn in state-governmental tax receipts between 2012 and 2020. An exact valuation of the market remains elusive, however, given the various factors used to determine that valuation — the number of Internet poker licenses on offer, say, or the tax rate applied to an operator's Internet poker proceeds — have still to be settled upon by lawmakers.

Current Status

Two Internet poker bills — **SB51** (A, at right), introduced on Dec. 19, 2012, and **SB678** (B, at right), introduced on Feb. 23, 2013 — are pending in the Senate. They are sponsored by Democratic state Senators Roderick Wright and Lou Correa, respectively. The two bills have seen no action, as, separately, two influential tribal gaming coalitions have been busy hammering out a substitute Internet poker measure. On May 13, eight tribal governments publicized a **draft Internet poker proposal** (C, at right). It is supported chiefly by the Pechanga Band of Luiseño Indians and is intended as an alternative to SB51 and SB678. Separately, 15 tribal governments are imminently expected to release a similar draft Internet poker proposal. It is supported mainly by the San Manuel Band of Mission Indians and is intended as an alternative to SB51. Both tribal coalitions want, among other things, tribal governments to serve as Internet poker regulators.

Timeline

SB51 and SB678 are pending in the Senate Governmental Organization Committee, which Wright chairs. Hearing dates have not been set. The Pechanga and San Manuel draft proposals have not been introduced but may debut imminently, sources said.

Quick Facts

Gaming Activity Allowed	
(A, B, C) Internet Poker	✓
Internet Casino or Bingo	
Internet Lottery	
Regulation	
(A, C) Intrastate	✓
Interstate	
Operator Licensing	
Monopoly	
(A, C) Land-Based Incumbents	✓
Open	
Supplier Licensing	
Non-Restricted	
(A, C) Restricted	✓
Regulator	
(A, C) Gambling Control Commission	✓
(A, C) Department of Justice	✓
(C) Tribal Gaming Regulators	✓
Age Requirement	
18 Years or Older	✓
(A, C) 21 Years or Older	
Advertising Permitted	
(A, C) Yes	✓
No	
Tax Rate	
(A) 10% of GGR	✓
(B, C) TBD	✓

MASSACHUSETTS (PENDING)

Overview

Massachusetts is considered one of the largest prospective Internet gambling markets in the United States given its population, approximately 6.5m residents, is among the highest in the nation. An exact valuation of the market, however, has not been made public by private or governmental sources.

Current Status

An Internet gambling bill, **S101** (A, at right), was introduced on Jan. 22, 2013. It is sponsored by Democratic state Sen. Jennifer Flanagan and would authorize the lottery to offer online games. The bill does not specify which games would be authorized. But if permitted, the lottery intends to offer a limited number of ticket games on a pilot basis, lottery officials told GamblingCompliance in late January. Other games, including keno, would come later. Separately, another bill, **S197** (B, at right), was introduced on Jan. 22. It is sponsored by Republican state Sen. Bruce Tarr and would authorize the state's prospective casino and slot-parlor license holders to offer Internet gambling. Although the bill does not specify which games would be authorized, it does specify which would be prohibited: (i) games that the lottery is already running and (ii) games that simulate or resemble slot machines. Meanwhile, Internet poker language was introduced as **Amendment No. 365** to **H3400**, the House budget bill, in early April. The amendment was sponsored by Republican state Rep. Bradley Jones and would have authorized up to three Massachusetts-based entities to operate intrastate poker websites. The amendment was removed from H3400 on April 24.

Timeline

S101 is pending in the Joint Committee on Consumer Protection and Professional Licensure. S197 is pending in the Joint Committee on Economic Development and Emerging Technologies. Hearing dates for the bills have not been set. The bills face no deadlines this year.

Quick Facts

Gaming Activity Allowed

Internet Poker	
Internet Casino or Bingo	
Internet Lottery	

Regulation

Intrastate	
Interstate	

Operator Licensing

(A) Monopoly	✓
(B) Land-Based Incumbents	✓
Open	

Supplier Licensing

Non-Restricted	
Restricted	

Regulator

(A) Lottery Commission	✓
(B) Gaming Commission	✓

Age Requirement

18 Years or Older	
21 Years or Older	✓

Advertising Permitted

Yes	
No	

Tax Rate

(A) Tax-Exempt State Corp.	✓
(B) TBD	✓

PENNSYLVANIA (PENDING)

Overview

Pennsylvania is considered one of the largest prospective Internet gambling markets in the United States given its population, approximately 12.7m residents, is among the highest in the nation. An exact valuation of the market, however, has not been made public by private or governmental sources.

Current Status

An Internet gambling bill, **HB1235** (at right), was introduced on April 18, 2013, and is sponsored by Democratic state Rep. Tina Davis. Under HB1235, Internet gamg includes table games, slot-style games and other games as approved by the Pennsylvania Gaming Control Board. Any slot-machine licensee who obtained an "Internet gaming certificate" from the Board would be permitted to operate Internet gaming. The bill is silent as to potential restrictions on off-shore operators. Daily Internet gaming gross revenue would be subject to a 28 percent tax. Players must be at least 21 years of age to wager and accounts must be initially established on the premises of a licensed facility. Interstate or international play may be permitted if such wagers are (i) not inconsistent with federal law or regulation; (ii) not inconsistent with the law of the jurisdiction in which the player is located, including foreign jurisdictions; and (iii) play is conducted pursuant to an interstate compact or reciprocal agreement. Separately, a bill that would prohibit Internet gambling, **HB1404**, was introduced on May 15 and is sponsored by Republican state Rep. Paul Clymer.

Timeline

HB1235 is pending in the House Gaming Oversight Committee. But Republican Tina Pickett, the committee chairwoman, said in early June that the bill is not expected to move this year. Meanwhile, Republican state Sen. Robert Tomlinson has circulated draft Internet gambling legislation but, according to sources, is taking a "deliberative" approach and is in no hurry to introduce it.

Quick Facts

Gaming Activity Allowed	
Internet Poker	✓
Internet Casino or Bingo	✓
Internet Lottery	
Regulation	
Intrastate	✓
Interstate	✓
Operator Licensing	
Monopoly	
Land-Based Incumbents	✓
Open	
Supplier Licensing	
Non-Restricted	✓
Restricted	
Regulator	
Gaming Control Board	✓
Age Requirement	
18 Years or Older	
21 Years or Older	✓
Advertising Permitted	
Yes	
No	
Tax Rate	
28% of GGR	✓

FEDERAL (PENDING)

Overview

The United States is considered one of the world's largest Internet gambling markets. A 2011 white paper released by the American Gaming Association estimated that Internet poker alone could generate around $2bn in federal-governmental tax receipts, annually. An exact valuation of the market remains elusive, however, given the various factors used to determine that valuation — the number of participating states, say, or the tax rate applied to an operator's Internet poker proceeds — have still to be settled upon by lawmakers.

Current Status

An Internet gambling bill, **HR2282**, was introduced on June 6, 2013. It is sponsored by Republican Rep. Peter King of New York. The bill would establish a federal regime for regulating all forms of Internet gambling. It would also allow states already running Internet gambling to continue doing so under the federal regime. The Treasury Department would serve as federal regulator but would also be tasked with selecting qualified state and tribal bodies that would assist with Internet gambling regulation. The bill requires that U.S. state and tribal jurisdictions opt in to the federal regime before licensed operators can accept wagers from players located in those jurisdictions. A state or tribe is considered opted-in unless the appropriate state or tribal official notifies Treasury otherwise within 120 days of enactment. The bill would make it unlawful for any person to operate Internet gambling unless authorized in accordance with its provisions.

Timeline

HR2282 is pending in multiple House committees. It is not expected to move, sources said, and no hearing date has been set. A separate Internet poker bill sponsored by Republican Rep. Joe Barton of Texas is expected to debut this summer. Sources said the two bills are merely intended to keep Internet gambling on the congressional radar.

Quick Facts

Gaming Activity Allowed	
Internet Poker	✓
Internet Casino or Bingo	✓
Internet Lottery	
Regulation	
Intrastate	
Interstate	✓
Operator Licensing	
Monopoly	
Land-Based Incumbents	
Open	✓
Supplier Licensing	
Non-Restricted	✓
Restricted	
Regulators	
Treasury Department	✓
Qualified State/Tribal Bodies	✓
Age Requirement	
18 Years or Older	
21 Years or Older	✓
Advertising Permitted	
Yes	
No	
Tax Rate	
N/A	

DEAD LEGISLATION

Hawaii

On Jan. 18, 2013, an Internet gambling bill, **SB678**, was introduced in the Senate. It was sponsored by Democratic state Sen. Malama Solomon and would have authorized the Hawaii Internet Lottery and Gaming Corporation to operate an intrastate and interstate gambling website. It died on March 1, after failing to meet a committee deadline.

Iowa

On Jan. 23, 2013, an Internet poker bill, **SSB1068**, was introduced in the Senate. It was sponsored by Democratic state Sen. Jeff Danielson and would have authorized Iowa-based casinos to operate intrastate and interstate poker websites. It died on March 8, after failing to meet a committee deadline.

Texas

On March 5, 2013, an Internet poker bill, **SB1103**, was introduced in the Senate. It was sponsored by Democratic state Sen. Leticia Van de Putte and would have authorized the Texas Lottery to participate in a future federal Internet poker regulatory program. A companion bill, **HB3529**, was introduced by Republican state Rep. John Kuempel on March 8. The bills died in session. The Texas Legislature adjourned on May 27 and will not convene again until 2015.

Illinois

On March 6, 2013, Internet gambling language was introduced as **Amendment No. 1** to **SB1739**, a Senate bill. It was sponsored by Democratic state Sen. John Cullerton and would have authorized Illinois-based casinos, electronic gaming machine operators and advance-deposit wagering firms to operate intrastate and interstate gambling websites. Amendment No. 1 was removed from SB1739 on May 1. A Cullerton spokesman told GamblingCompliance in mid May that Cullerton will push the Internet gambling language as a standalone bill "as soon as we get the votes."

Mississippi

On Jan. 14, 2013, an Internet gambling bill, **HB254**, was introduced in the House. It was sponsored by Democratic state Rep. Bobby Moak and would have authorized Mississippi-based casinos to operate intrastate gambling websites. It died on Feb. 5, after failing to meet a committee deadline.

U.S. INTERNET GAMBLING LEGISLATIVE PROGRESSION MONITOR

		HOUSE			SENATE			
BILL		COMMITTEE	FLOOR	CONFERENCE	FLOOR	COMMITTEE	ENACTED	SIGNED
CA	SB51					✓		
CA	SB678					✓		
HI	SB768					✓		
IA	SSB1068					✓		
IL	SB1739				✓	✓		
MA	S101					✓		
MA	S197					✓		
MS	HB254	✓						
NV	AB114	✓	✓		✓		✓	✓
NJ	A2578		✓		✓		✓	✓
TX	SB1103					✓		
TX	HB3529	✓						
PA	HB1235	✓						
PA	HB1404	✓						
FED	HB2282	✓						

● Approved ● Pending ● Dead

U.S. INTERNET GAMBLING REFERENCE TABLE

JURISDICTION	DE	NV	NJ	USVI	CA	MA	PA	FED	HI	IA	IL	MS	TX
GAMING ACTIVITY													
Poker	✓	✓	✓	TBD	✓		✓	✓	✓	✓	✓	✓	✓
Casino/Bingo	✓		✓	TBD			✓	✓	✓		✓	✓	
Lottery	✓			TBD					✓				
REGULATION													
Intrastate	✓	✓	✓	✓	✓		✓		✓	✓	✓	✓	
Interstate	✓	✓	✓	✓			✓	✓	✓	✓	✓		✓
OPERATOR LICENSING													
Monopoly	✓					✓			✓				
Incumbents		✓	✓		✓	✓	✓			✓	✓	✓	
Open				✓				✓					
SUPPLIER LICENSING													
Restricted		✓			✓				✓	✓	✓		
Non-Restricted	✓		✓	✓			✓	✓				✓	
TAX RATE													
	33.9% of Table Game Proceeds; 56.5% of Video Lottery Poceeds	6.75% of GGR	17.5% or 20% of GGR	1.5% GGR	10% of GGR		28% of GGR		Tax-Exempt State Corp.	22%-24% of GGR	15% of fee-based GGR; 20% of non-fee-based GGR	5% of GGR	
REGULATOR													
	Lottery	Gaming Commission; Gaming Control Board	Div of Gaming Enforcement; Casino Control Commission	Casino Control Commission	Gambling Control Commission, Dept. of Justice; Tribal Gaming Regulators	Lottery Commission; Gaming Commission	Gaming Control Board	Treasury Dept.; Qualified State and Tribal Bodies	Internet Lottery and Gaming Corp.	Racing and Gaming Commission	Lottery	Gaming Commission	Lottery Commission; Federa Agency TBD

● Internet gambling regulated ● Internet gambling legislation pending ● Internet gambling legislation dead

INTERNET LOTTERY TICKET SALES ACTIVITY MONITOR

The failure of federal Internet gambling legislation to advance in 2012 has positioned lotteries to exploit Internet gaming opportunities. Multiple lotteries have expressed an Interest in selling lottery games over the Internet. To date, only two, Georgia and Illinois, have begun selling tickets. Meanwhile, five others, Minnesota, New Hampshire, New York, North Dakota and Virginia, offer lottery subscription packages on their websites. The tables below highlight jurisdictions in which Internet lottery gaming is currently authorized and jurisdictions in which noteworthy developments have recently occurred.

INTERNET LOTTERY TICKET SALES LIVE			
Georgia	Internet sales of some draw tickets commenced on Nov. 25, 2012. Unlike Illinois, Internet ticket sales did not require authorizing legislation; instead, state officials determined that Georgia law already gives the lottery authority over the manner of ticket sales. See, **G.A. Code Ann. §§ 50-27-9(18), 50-27-10(2)**. The sale of draw tickets is "phase one" of the lottery's Internet gaming strategy, lottery officials said. The lottery hopes to implement "phase two" sometime in summer 2013, although no firm timeline has been set. "Phase two" is likely to consist of lottery games, such as keno, as well as a new type of instant ticket-based game, officials said.	**Authorized Games** Draw Tickets Other Lottery Games **Payment Methods** Pre-Paid Card Required	 ✓ ✓ ✓
Illinois	On March 25, 2012, the lottery began selling certain draw tickets, such as Mega Millions, over the Internet. The sales commenced pursuant to a pilot program, originally approved in 2009. The Internet sales pilot program must last for at least 36 months, but no longer than 48 months. Any changes to the pilot program, including the addition of new games or an extension of time, require express legislative authorization. **20 ILCS 1605/7.12**.	**Authorized Games** Draw Tickets Other Lottery Games **Payment Methods** Pre-Paid Card Required	 ✓

INTERNET LOTTERY TICKET SALES ACTIVITY MONITOR

NOTEWORTHY INTERNET LOTTERY DEVELOPMENTS	
Delaware	In June 2012, the Delaware Gaming Competitiveness Act was signed into law. One of the law's provisions allows for Internet ticket games. Internet ticket games are lottery games "in which the winner is decided by chance through mechanical or electronic means," including keno but not including video lottery, table games and other forms of Internet lottery. **29 Del. C. §4803(i)-4803(x)**. A go-live date for ticket sales has not been set.
Florida	In mid January 2013, two identical bills, **SB266** and **HB275**, were introduced in the Florida Legislature. The bills would have granted the Florida Lottery the ability to implement Internet ticket sales, after adopting the appropriate rules. Both measures died in committee on May 3.
Kentucky	On March 22, 2013, the Kentucky Lottery Corporation board of directors approved a plan to offer Internet-based sales of lottery tickets. In a **press release**, Arch Gleason, the lottery's president and chief executive, stated that the lottery planned to offer draw games, like Powerball and Mega Millions, before gradually moving into simulated scratch and instant-win games. Internet sales could be fully implemented in FY 2015, according to the release. Projected sales are $4.5m in the first year, growing to an estimated $31m by FY 2020.
Maryland	On Sept. 19, 2012, the Maryland Lottery issued a **report** on a proposed platform and regulatory structure for Internet lottery sales. In the report, the lottery noted its desire to sell traditional lottery products over the Internet. However, the lottery's plan prompted concerns from retailers, causing $400,000 originally budgeted to develop a website in FY 2014 to be removed from the lottery's budget. In addition, a bill to prohibit the lottery from selling tickets over the Internet, **SB272**, passed the Senate in late February but failed to come up for a vote in the House before the session ended on April 8, 2013.
Massachusetts	On Dec. 13, 2012, the Online Products Task Force, composed of state and industry representatives, issued a report that made several recommendations as to Internet gambling. Among them was a recommendation to allow the lottery to sell products over the Internet, including ticket games. Pursuant to the report, **S101** is currently pending. The bill would allow the lottery to conduct lotteries "online and over the Internet." The bill's sponsor, Democratic state Sen. Jennifer Flanagan, said it is intended as a "conversation starter" and is not final. Separately, **S197**, a measure to allow the state's prospective casino and slot-parlor license holders to offer Internet gaming, is also pending.
Michigan	On Jan. 8, 2013, the Michigan Lottery issued an RFP seeking a technology partner to provide "iLottery services." The planned expansion would include instant games, keno and bingo, as well as draw-ticket sales. The lottery's plan has sparked pushback from Michigan gaming interests, including lottery retailers, as well as state officials. In early April, companion measures, **SB294** and **HB4531**, which would prohibit Internet lottery sales, were introduced. Since then, neither bill has moved. Meanwhile, the Legislature in late May debated iLottery as part of broader talks on the state budget. Ultimately, no funds for iLottery implementation were set aside in the budget. The lottery is continuing to work with the Legislature on a move-forward solution for iLottery, a lottery spokesperson said in early June.
New Jersey	There are currently two bills pending in New Jersey to allow for lottery ticket sales over the Internet: **S56** would permit the lottery to conduct games over the Internet, and **A1073** would direct the state Lottery Commission to permit the purchase of lottery tickets by electronic means. Similar bills have been introduced before, without significant movement.
Oklahoma	On Jan. 17, 2013, Republican state Sen. Clark Jolley introduced **SB955**, which, among other things, would have prohibited a lottery game played using the Internet without purchase of a paper ticket from a lottery retailer on that retailer's premises. The measure passed the Senate in February, only to be stopped in the House in late April.

INTERNET LOTTERY TICKET SALES ACTIVITY MONITOR

NOTEWORTHY INTERNET LOTTERY DEVELOPMENTS	
Pennsylvania	A private management contract between Pennsylvania and lottery vendor Camelot was agreed in January and included provisions covering Internet gaming. In mid February, however, the contract was rejected by state Attorney General Kathleen Kane. Meanwhile, Republican State Sen. Robert Tomlinson is expected to introduce legislation that, among other things, would prohibit the lottery from offering Internet games that simulate casino-style gaming.
Vermont	In May 2012, language requiring the lottery to study "the option of allowing the sale of lottery tickets online" was enacted as part of the state's **budget bill**. **Findings** were delivered to state officials in mid January 2013. Chiefly, the lottery recommended that the state oppose any federal moves that would hinder it or other state lotteries from expanding online. The lottery also recommended that the state further study Internet lottery ticket sales and Internet gaming before moving ahead with its own online program.

NOTE:
This is not an exhaustistive list of all lotteries that are considering Internet gaming. Officials in multiple states not listed here have expressed an interest in exploring Internet gaming. This list is meant only to highlight various developments, particularly: (i) the issuance of a tender; (ii) the conduct of a state-mandated study; or (iii) the formal consideration of legislation or regulations.

STATES WHERE INTERNET GAMBLING IS PROHIBITED

Currently, nine states have express prohibitions targeting Internet gambling. In Texas, a bill is pending that would exclude "Internet poker" from the proposed definition of "poker" or "poker game." Prohibitions vary significantly from state to state, with some making exceptions for various activities. While most states do not have express prohibitions, general bans on gambling may be applied to Internet gambling. For this report, Internet gambling restrictions that may be included in state administrative regulations or tribal-state gaming compacts have not been considered.

ILLINOIS — ENACTED: 1997

The state of Illinois makes it a felony to knowingly establish, maintain or operate "an Internet site that permits a person to play a game of chance or skill for money or other thing of value by means of the Internet or to make a wager upon the result of any game, contest, political nomination, appointment, or election by means of the Internet." **70 ILCS 5/28-1(a)(12)**. Lotteries conducted by the state in accordance with the Illinois Lottery Law, **20 ILCS 1605/7.12**, are exempted from this prohibition. **70 ILCS 5/28-1(b)(6)**.

INDIANA — ENACTED: 2005

The Indiana Criminal Code provides that "An operator who knowingly or intentionally uses the Internet to engage in unlawful gambling… in Indiana; or…with a person located in Indiana; commits a Class D felony." **IC 35-45-5-2(c)**. A 1998 State Attorney General Opinion discusses the scope of illegal Internet gambling and Indiana state laws. The opinion provides further clarity not only on how a gaming operator may violate the law by utilizing the Internet but how an individual gambling in Indiana may also violate the law.

LOUISIANA — ENACTED: 1997

Gambling by computer, meaning "the intentional conducting, or directly assisting in the conducting as a business of any game, contest, lottery, or contrivance whereby a person risks the loss of anything of value in order to realize a profit when accessing the Internet, World Wide Web, or any part thereof by way of any computer, computer system, computer network, computer software, or any server" is prohibited in Louisiana. **LARS 14:90.3(B)**.

MONTANA — ENACTED: 2005

Except as specifically authorized by the state, all forms of gambling are prohibited, including Internet gambling. **MCA 23-5-112(19)(e) and (21)(a)** and **MCA 23-5-151**. However, that prohibition does not include: (1) the operation of a simulcast facility or advance deposit wagering as explicitly licensed under **MCA 23-4**; (2) any state lottery operations expressly noted in **MCA 23-7**; and (3) Indian gaming conduced on Indian land in conformity with federal law. **MCA 23-5-112(21)(b)**. Conducting a fantasy sports league or selling raffle tickets over the Internet is expressly barred. **MCA 23-5-802** and **MCA 23-5-413(3)(b)**.

NEVADA — ENACTED: 2001

Compared to the other states that maintain prohibitions against some form of Internet gambling, Nevada's are the most complex. Generally speaking, unless specifically provided in another Nevada statute, **NRS 465.092** and **465.091** makes Internet wagering a misdemeanor. There are multiple exceptions to the statute, including exceptions for Internet poker, mobile sports betting and pari-mutuel wagering.

OREGON — ENACTED: 2001

Oregon's Internet gambling ban prohibits financial transactions involving Internet gambling. In sum, a person involved in an Internet gambling business cannot knowingly accept credit cards, ETF transfers, checks, or other financial instruments in connection with the participation of a person in unlawful gambling over the Internet. **ORS 167.109**.

STATES WHERE INTERNET GAMBLING IS PROHIBITED

SOUTH DAKOTA

ENACTED: 2000

Under South Dakota law, no person may establish a location or site in the state "from which to conduct a gambling business on or over the Internet or an interactive computer service." **SDCL 22-25A-8**. However, that prohibition does not apply to South Dakota Gaming Commission or the state lottery as to activities expressly authorized. **SDCL 22-25A-15**.

UTAH

ENACTED: 2012

Utah prohibits all forms of gambling. Utah Criminal Code, **76-10-1101** and **76-10-1002**, states that anyone who "intentionally provides or offers to provide any form of Internet or online gambling to any person" in Utah is guilty of a misdemeanor. The law provides an exemption from liability for Internet service providers and other similar entities that store, transmit or route data to facilitate the distribution of content over the Internet, but that do not exercise control over such content.

WASHINGTON

ENACTED: 2006

It is a felony in Washington to knowingly transmit or receive gambling information via the Internet, or to knowingly install or maintain equipment for the transmission or receipt of gambling information, with the exception of licensed pari-mutuel wagering on horse racing. **RCW 9.46.240** and **WAC 206-49**. Of note, the legislative comments to the law state "It is the policy of this state to prohibit all forms and means of gambling, except where carefully and specifically authorized and regulated."

GLOSSARY OF KEY TERMS

Dead: Internet gambling legislation is no longer pending.

GGR: Gross gambling revenues.

Land-Based Incumbents: Operator licensing is open only to land-based incumbents in that jurisdiction.

Monopoly: Operator licensing is open exclusively to a state-run entity or concessionaire.

Non-Restricted: Supplier licensing is not expressly closed to applicants that took or facilitated the taking of U.S. wagers before applying for a license.

Open: Operator licensing is open to most or all applicants.

Operator: A gambling business that transacts directly with consumers.

Pending: Internet gambling legislation is pending.

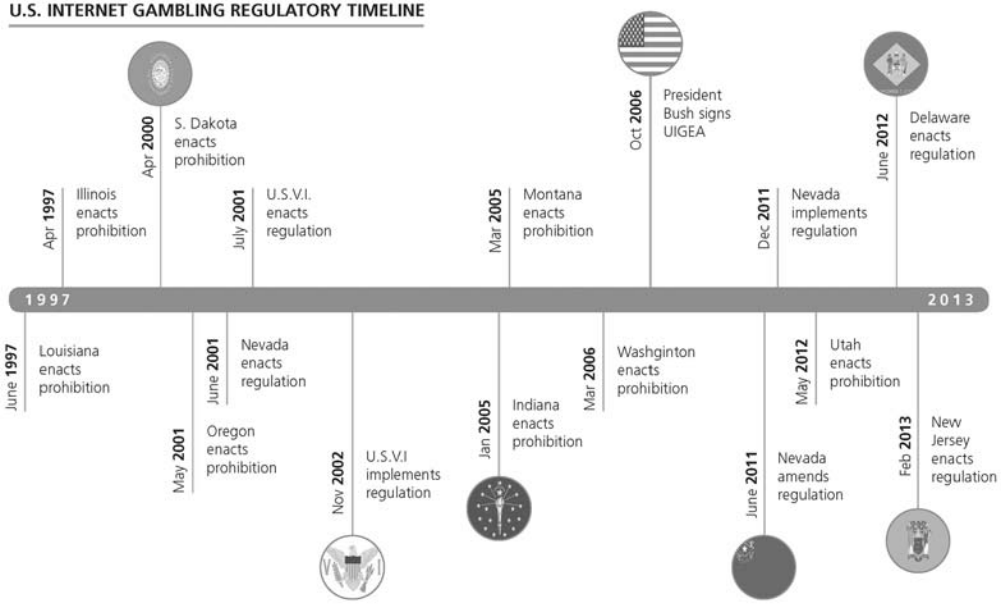
Regulated: Internet gambling is regulated.

Restricted: Supplier licensing is expressly closed, either temporarily or indefinitely, to applicants that took or facilitated U.S. bets before applying for a license.

Supplier: A business that provides gambling software to an operator.

Third-Party Service Provider: A business that provides payments, geo-location, identity-verification or other ancillary services to an operator.

U.S. INTERNET GAMBLING REGULATORY TIMELINE



APPENDIX: 2012 U.S. INTERNET GAMBLING REFERENCE TABLE

JURISDICTION	DE	NV	USVI	NJ	FEDERAL	REID-KYL	CA	HI	IA	IL	MA	MS	PA
GAMING ACTIVITY													
Poker	✓	✓	TBD	✓	✓	✓	✓	✓	✓		✓	✓	✓
Casino/Bingo	✓		TBD	✓	✓			✓				✓	✓
Lottery	✓		TBD		✓			✓					
REGULATION													
Intrastate	✓	✓	✓	✓			✓	✓	✓	✓	✓	✓	✓
Interstate	✓		✓	✓	✓	✓		✓	✓	✓			
OPERATOR LICENSING													
Monopoly	✓							✓		✓			
Incumbents		✓		✓	✓	✓	✓		✓	✓		✓	✓
Open			✓		✓						✓		
SUPPLIER LICENSING													
Restricted					✓	✓	✓	✓	✓		✓		
Non-Restricted	✓	✓	✓	✓	✓					✓		✓	✓
TAX RATE													
	33.9% of Table Game Proceeds; 56.5% of Video Lottery Poceeds	6.75% of GGR	1.5% of GGR	15% of GGR	2% of Customer Deposits	16% of Internet Poker Receipts	10% of GGR	Tax-Exempt State Corporation	22%-24% of GGR	Tax-Exempt State Corporation; Internet Gaming Affiliates TBD	25% of GGR	5% of GGR	45% of GGR
REGULATOR													
	Lottery	Gaming Commission; Gaming Control Board	Casino Control Commission	Div. of Gaming Enforcement; Casino Control Commission	Treasury Secretary; Commerce Secretary; Qualified State/Tribal Agencies	Commerce Secretary; Qualified State/Tribal Agencies	Gambling Control Commission; Dept. of Justice	Internet Lottery and Gaming Corporation	Racing and Gaming Commission	Lottery	Gaming Commission	Gaming Commission	Gaming Control Board

● Internet gambling regulated ● Internet gambling legislation pending ● Internet gambling legislation dead

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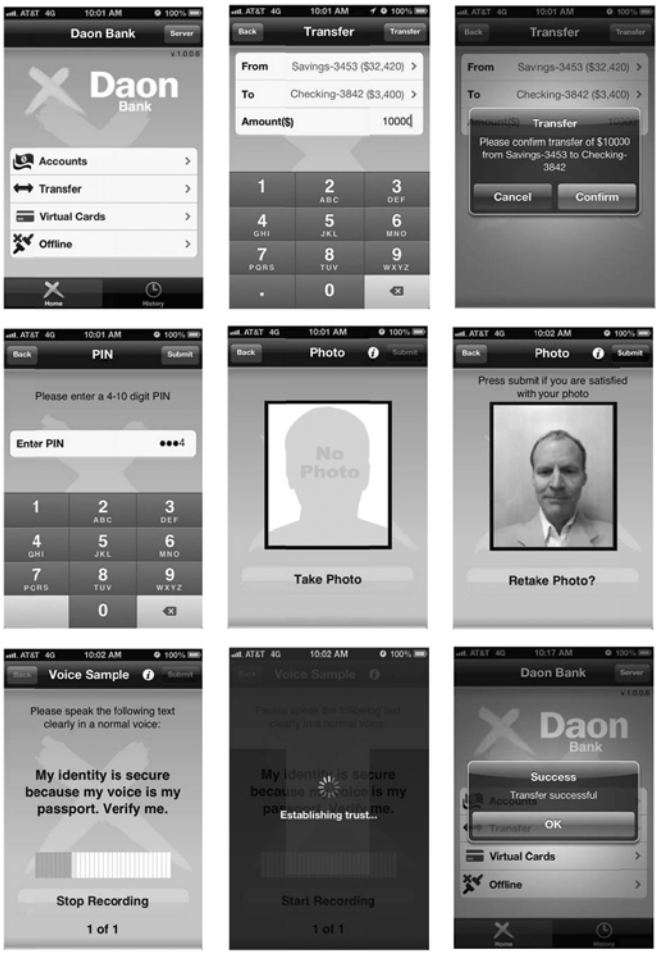
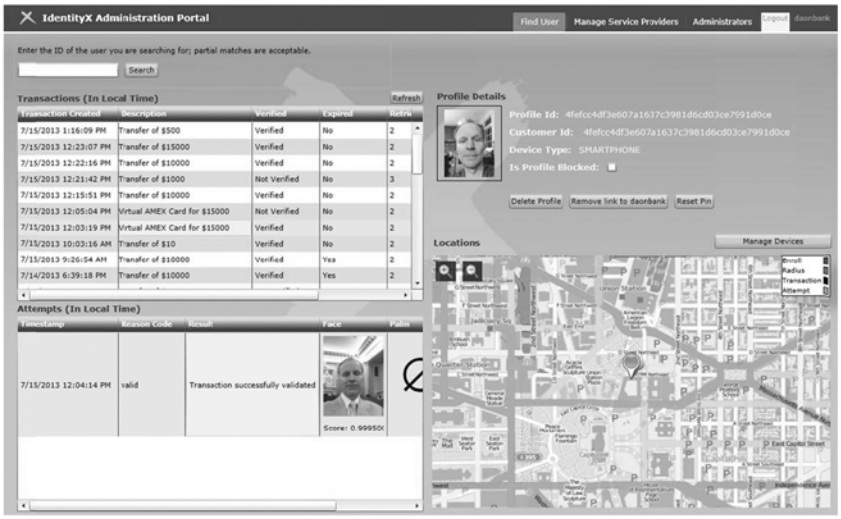
IdentityX – Smartphone App – Exhibit B



IdentityX - Command Center



Senator MCCASKILL. Thank you. It is fascinating, but clearly this has not been adapted mainstream yet. I am not aware of anywhere that I do business that this technology is available.

So, the first question that comes to mind is, let us assume that there are online gaming entities that are identified and by state gaming authorities or, if we do Federal regulations, Federal gaming authorities. Is it your testimony that what we do is require that the only way you could do online gaming would be if, A, the online gaming entity had this technology, and, B, the people who wanted to play poker online would have to have an iPad that could take their picture and listen to their voice, or a computer that would do that?

Mr. GRISSEN. Sure, two great questions. The first question is related to the awareness of it, the technology is in the marketplace. As we speak, it is being rolled out by banks. It is being distributed in consumer security marketplaces in 15 countries around the world, 17 languages. It is part of the NIST program with the Department of Commerce, the National Strategy for Trust Identities in Cyberspace.

And the second part of the question is, would we require it. Biometrics are a very powerful tool, and it would be my recommendation that these types of technologies should be adopted as they are being adopted in other industries. And it does not require an iPad. It could be any device: Android, Apple, tablet, or smartphone. It would require a device with the capabilities to have a camera, which most do, have location-based capabilities within them, and a microphone.

Senator MCCASKILL. Well, it certainly adds a new wrinkle to the gazillion people who have tweeted at me over the last 10 days. I do not know how they are all going to feel about not being able to

play online poker if they are not willing to take their picture every time they log in. And so, you are going to have some real friction between—because a lot of the people who want to play online poker are attracted to it because they do not want to do it in public. They do want to go to a brick and mortar place either for the convenience or for the privacy.

So it is a fascinating—you know, obviously I am respectful of the technology, but the question is, it creates a real friction between those people who want privacy in this age that we are talking about, big data, and we are talking about NSA capabilities, and we are talking about what people know about you based on what you click, or whether you have GPS on. It is fascinating that we would open a whole new treasure trove of data. And I trust that you say that it is encrypted.

But do any of the three of you have a comment on this as to whether or not you think this technology would alleviate some of the concerns that you have expressed about online gaming, particularly as it relates to the people that will flock to this in order to make a quick dollar, and then switch an ID address?

Mr. BLUM. I think that identifying who the customer is is very important. It is part of money laundering rolls. But the reason you have to know your customer regulations in the banking system is to be able to figure out whether the transactions that are going forward are appropriate or not. And this does not begin to address that kind of question.

So a bank wants to know who you work for, what are your usual deposits, what kind of usual activity goes on in your account. This would tell you, yes, that is the guy, but it will not tell you anything about how that account might be used or what is an appropriate level of use. So if someone wants to put $10,000 or $20,000 or $50,000 on account with a casino, how do we know that that person is an appropriate person to be putting it there? And how do we know that they are going to gamble it and not move it around to some other location?

I do not think that this solves that problem. You really need an anti-money laundering regime in the casino to make it work.

Senator MCCASKILL. Anybody else? Senator Heller?

Senator HELLER. Thank you. A few years ago—actually, more than a few years ago when I was Secretary of State, I got a phone call from a colleague of mine on the East Coast, another secretary of state. And the purpose of that phone call was to tell me that his son had left for college, and that he got onto a website for gambling and had gambled away his tuition. And you can imagine the parent was not happy about this, less happy about the fact that when he pulled up the website it said "Las Vegas" on it. And it was not a Las Vegas website. They just knew if you put "Las Vegas" on the site, that that would be more attractive, but it was an offshore site.

This parent, I sent them to the Gaming Control Board, and how that ended up at the end of the day I really do not know. But I doubt that it worked out as well as he would have hoped that it would have worked out.

And I am sure that for those sitting on this panel and those who were serving in Congress at the time, this was not a rare phone call. I am sure that many parents had the same problem, same

issues, and for that reason, Congress made certain steps, certain procedures, to make—to bring this to an end. And I think UIGEA is one of those fixes, and it would have made sense, especially in this case, where it was prior to this action taking place, that they could monitor these transactions through financial institutions, and be able to bring it to a halt from unusual transactions that occur in these accounts.

And the reason we are here today is—and I emphasized this in my opening remarks, but I continue to want to reemphasize this—is that on December 23, 2011, the Administration changed all this, changed it all. And the reason that the Administration changed this was so that their friends in Illinois and New York could put their lottery tickets on line. So unilaterally, the White House made a decision 2 days before Christmas when all of us were out of town, not calling a single Member of Congress, said we are going to change the way we do business here in this country, and we are going to exempt Internet gaming, and we are going to say that it only pertains to sports betting. And that is why we are here having this discussion, this meeting here today.

As I mentioned, five states now have approved it for their states. Twenty states are looking at it now in how to move forward on what may be this new source of revenue. And here is my concern. I have an iPad here in front of me, and I have a gambling site on it. And this is what is going to happen a few years down the road.

Some parent is going to see their 14-year-old child on an iPad, and they are going to be gambling. That child is going to be gambling. And they are going to say, wait a minute, what just happened? They have no idea that this is coming down the road because it is going to be so difficult to determine who that person is, what age they are, and where they are. They are not going to be able to handle that.

And because of the actions of this White House is why we are where we are today for what I define as friends making—helping friends and making sure that some of these states could put their lottery tickets online. And it concerns me.

I want to thank all the witnesses here for taking time, and it was very, very helpful.

I want to start with you, Mr. Canterbury. And taking a look at what we are doing and what we are trying to define here, what actions does this Congress need to take? What do we need to reverse? Is there something beyond just reversing the actions of the White House, or is there more that we can do to assist you and your organization, making sure that we can stop children and perhaps problem gamblers from getting caught up in this web?

Mr. CANTERBURY. Philosophically, with law enforcement, obviously we are always behind the eight ball on the technology, especially at the state and local level. It will take us years to get to the place that we need to be technologically to fight any kind of money laundering at a state level that progresses, especially when it is cross-border money laundering. State and local law enforcement just will not have the resources to do it.

The interpretation by the Justice Department obviously does not concur with what we felt Congress passed prior, so we believe that there does need to be a congressional fix. And, you know, the FOP

has not taken a position pro-gambling or anti-gambling. I mean, anything that generates revenue for state and local government, I am for it because that is where all of my members get their paychecks. So we are very concerned about the revenue aspect. But we also know that the terrorist groups have been using any kind of Internet sales, not just gambling, to try to launder money.

So anything that Congress can do, and obviously we stand ready to work with the Senate to develop that technology. But philosophically, the fix would help us immediately. The technology that we have seen here today, I am not sure, as Mr. Blum said, that it would prevent the money laundering, but it does help with respect to underage gambling and troubled gaming, because almost every crime that you see associated with gambling is associated with the debt.

Senator HELLER. Mr. Grissen, do you monitor every atate? If there are five states out there right now that have approved Internet gambling, there are 20 states that are looking at it. Have any of them submitted any legislation that would create the protections that you just shared with us? I mean, are they looking at this technology and trying to protect the most vulnerable?

Mr. GRISSEN. I am not an expert in online gambling or Internet gambling. To my knowledge, there are no states that are.

Senator HELLER. No states have contacted you?

Mr. GRISSEN. No. I believe that if they had the similar level of interest in this committee and technology ion looking at these things, that they would. I think there is a reluctance to move first.

In contrast, banking is using it to create differentiators and provide an enhanced trusted service with our customers. So I think it is somewhere in an adoption curve, but I have not seen any overtures to try and look aggressively at this technology.

Senator HELLER [presiding]. OK. I will save my questions as we get through the panel here. But, Senator Blunt?

Senator BLUNT. Thanks, Senator Heller, and thank you for your leadership on this. I would say to Mr. Canterbury that, you know, the interpretation that Justice made of the Wire Act certainly was not what we anticipated or had been the interpretation when the 2006 Act was passed. And that decision either totally and forever more changes the playing field on these issues, or Congress now has to go back as legislation could, and hopefully will do, and look at what we need to do now, based with this new interpretation of what the Wire Act means.

Mr. Canterbury, what is your sense of how important it is that there be one legal standard here as opposed to state by state or community by community standards?

Mr. CANTERBURY. I think it is important to have one Federal standard because you have 50 different State laws associated with gaming. For instance, in in my state, they are still arguing on legalizing raffles for churches, you know. There is very little. Our state lottery is the only thing that we have besides a little bit of charitable bingo.

And I know that there are absolutely no laws in South Carolina that would cover anything involving the Internet or the gaming industry on the Internet. So I believe it needs to be uniform. Law enforcement will not be able to attack money laundering and terrorist

activity using these funds with 50 laws. There needs to be one, and I think it needs to be enacted so that it will work well with the state laws. But I think it is going to have to be a Federal standard.

Senator BLUNT. Yes. Mr. Smith, from your testimony, my impression was that you do not think there could be a worse position than we are in right now, that this current regulatory position is the worst possible place to be.

Mr. SMITH. That is correct, Senator. And, you know, it is not the first time that Congress has heard about this. You have got the National Gambling Impact Study Commission report from 1999 where you had the state—the National Association of Trained Generals, keying off of what Chuck just said. We were talking about having a Federal standard.

The Attorney General at the time when Florida was mentioned, "State law prohibits an individual in Florida from placing a bet or wager by wire communication or by use of the Internet. However, the burgeoning of the Internet and the difficulty in adopting and implementing durable and effective enforcement mechanism makes any effort to regulate Internet's use better suited to Federal legislation rather than a patchwork attempt by individual states." And he said that in 1997.

And so, this new interpretation of the Wire Act that was a Christmas present from the Administration just sets us back.

Senator BLUNT. Right. Mr. Blum, I had a Children's Hospital meeting that I needed to step into, so I did not get to hear your testimony. It is available to us, and I have some sense of what was in it. But on money laundering, I mean, your sense would be, what, that the more outside unregulated contacts there are, the more you create vulnerability to both your money that you have and money that other people have that they want to send somewhere?

Mr. BLUM. The problem is you have got to know who owns the casino. You have got to know that the money coming into the casino is, in fact, gambling money, and that the profits of the casino are a disguised way of hiding proceeds of crime. So that means some kind of licensing for the casinos. It means an auditing of the casinos to see that what is going on somehow relates to the profit they are declaring, and that that money, in fact, is taxed, and the people who are in the gaming situation pay taxes. All of this is taken care of for the bricks and mortar institutions.

The only way you can do that on the Internet is to have a uniform Federal standard and to have some Federal agency that takes on this tax. The current situation is absolute open season, and I do not see how you can get it under control. No individual state government, to my knowledge, has the resources, or for that matter, the interest in pursuing individuals who violate state law by gambling on the Internet. It seems to me that that is way beyond the enforcement capacity of any state government.

Senator BLUNT. And you believe that the Internet—this gambling on there is being used aggressively as a money laundering tool by people who have money that they have through illegal purposes?

Mr. BLUM. Absolutely. My feeling about it is that this is a tool that is being used by people who want to launder money. You would not have service providers offering essentially complete soft-

ware packages to give you an online casino if somebody did not want to use the casino for nefarious purposes; that somebody in Bermuda says, hey, you want a casino? We have got three versions of it. You can set it up, put whatever name you want on it. And, by the way, it is going to be owned by a company that nobody can identify. To me, that is guaranteed trouble in the money laundering area.

Senator BLUNT. And you believe it is one of the top places people are laundering money right now?

Mr. BLUM. Absolutely. Absolutely. It has been for the longest time, and that is why it got regulated in the brick and mortar world.

Senator BLUNT. Right. Thank you, Mr. Heller.

Senator HELLER. Thank you. Senator Ayotte?

STATEMENT OF HON. KELLY AYOTTE,
U.S. SENATOR FROM NEW HAMPSHIRE

Senator AYOTTE. Thank you, Mr. Chairman. I want to thank the witnesses for being here. As I listen to this and I think about what the Attorney General did nearly 2 years ago where he rolled back 50 years of established law under the Wire Act basically with the stroke of a pen, what we have here is a free for all. I mean, this is a situation where we have got not only potential for money laundering, but let us be clear who can use this for money laundering. We can have organized crime do it, but we can also have terrorist organizations. Would that not be right, Mr. Canterbury?

Mr. CANTERBURY. I do not think there is any doubt about that, Senator.

Senator AYOTTE. And then, I look at the other issues created by this, not only money laundering, but I thought it was very telling in your testimony about the use also for drugs to basically—drug dealers, some of the issues happening in Costa Rica. I mean, this is deeply troubling. All the work that the police are doing every day on illegal drug interdiction, and then this is—this becomes a whole free for all without some Federal regulation of this.

And is this—we are already seeing this in terms of drug interdiction and the money laundering on that end?

Mr. CANTERBURY. That and prostitution. The recent arrests in Mexico, for example, it was forcing people to haul in money and/or drugs. And obviously the hauling of the money is just as—or more important to them than the hauling of the drugs. So, yes, I think it is.

Senator AYOTTE. Right. So, people are being trafficked over this as well.

Mr. CANTERBURY. Human trafficking is obviously part of this.

Senator AYOTTE. So, just to be clear, this is having a real human impact on people, and we have not even gotten into the addiction yet that can be created by gambling, and particularly with no—how are we making sure that children are not doing this at this point? The story that Dean talked about with someone who gambled away their college tuition, this is probably replicated across the Nation. Can you comment on that, Mr. Canterbury and Mr. Smith?

Mr. CANTERBURY. I think the only regulation now is when it says "are you over 18?" Yes.

Senator AYOTTE. Well, you know, my kids are pretty sharp. I do not think it would take them long to get around that at the age of five and eight, right?

Mr. CANTERBURY. Yes.

Mr. SMITH. I will go younger than that. My 3-year-old is already pretty sharp on devices.

Senator AYOTTE. And let us not kid ourselves. Our kids are a lot more tech savvy than we are, right?

Mr. SMITH. Well, and you saw with, you know, you have the Lehigh University student who, you know, served 22 months in prison because he got in such debt from online gambling, he tried to rob a Wachovia.

Senator AYOTTE. Have you looked at the issue, Mr. Smith, in terms of gambling addiction, whether online gambling actually—I could envision a scenario where it would be easier to become addicted to that because you can do it anywhere. And you do not have to be seen somewhere to do it. Have you looked at that piece of it?

Mr. SMITH. Yes, and actually there is a University of Buffalo research study into addiction, and they found that there is a problem of gambling among young people. And when there is an increase in gambling, there is reason to be concerned. And when you add access, it is not without gambling problems. And that goes to the pathological addiction issues.

Senator AYOTTE. So what happens to a state like mine where recently our State legislature made a policy decision that they did not want to expand gambling to have, for example, casinos in the state. And it was a bipartisan policy decision. I previously served as Attorney General of our state, so I dealt with these issues as well there.

How could it be possible in the current scenario that even the policy decisions that states like South Carolina make or New Hampshire are respected under this scheme, because could not just their residents just go online and do anything? It is a free for all without even really even any regulation on age that is verifiable. Mr. Blum, can you comment on that?

Mr. BLUM. I think for a state to try to enforce any rules with respect to Internet gambling is really a stretch. First of all, just consider the resources, and the time, and the effort, and the impossibility of building a case that you could actually prosecute.

States have a lot of law enforcement priorities. To go into this is really a big deal. And that is why it has to be regulated, and it has to be regulated at the Federal level.

Senator AYOTTE. Mr. Canterbury, you know, when I was AG, it was one of the areas that I know law enforcement did a lot of work in, but it was always a technological challenge. For example, Internet predators and fraud committed on the Internet, that was a challenge. So I can imagine with the technology challenges that law enforcement has on those types of cases that this really is beyond the reach of your average local law enforcement agency to be—if there were these types of crimes, money laundering is committed without Federal regulation of this. Would you agree?

Mr. CANTERBURY. Absolutely. I mean, at the state and local level, crime is prioritized, you know. We are going to respond to armed robberies and burglaries much faster than we are going to respond

to the call that there is a prostitute or my child gambled. I mean, there will be a response, but the ability of state and local law enforcement to go outside of their own jurisdiction to do anything when a child has gambled online in Myrtle Beach, where I am from, at a casino in Bermuda, there will be absolutely nothing that local law enforcement could do about that. That is why we believe it has to be dealt with at the Federal level.

Senator AYOTTE. Well, I appreciate all of you being here, and I want to thank the Chairman and the Ranking Member for having this hearing because shame on us if we do not get something done on this, because when I think about the possibility for money laundering, terrorism, drug trafficking, and the potential for children to get access and to use the Internet, as well as people to not deal with the addiction issue, I hope this is something that we move on very quickly. Thank you.

Senator HELLER. Thank you.

Senator Pryor?

STATEMENT OF HON. MARK PRYOR,
U.S. SENATOR FROM ARKANSAS

Senator PRYOR. Thank you, Mr. Chairman. I am just going to have a couple of questions. I think I will focus those on Mr. Smith, and then I'm going to get out of the way and let my other colleagues ask questions.

Mr. Smith, you rightly point out that the Congress has the duty to protect our children, and I think we do as well. And I am a big supporter of the unlawful Internet Gambling Enforcement Act. And I would like to get your thoughts on anything that can be done, say, in the area of advertising that, you know, advertising geared toward children that you would like to see us address and how you think we can do that. And I would just like to get your thoughts on that.

Mr. SMITH. OK. Are you speaking specifically for the gaming?

Senator PRYOR. Yes.

Mr. SMITH. That is a big challenge. Anybody that has played a game whether on an app, or on a desktop or laptop, or other handheld device, you are constantly seeing the pop up ads target the various phones. And to my knowledge, there is no screening mechanism. If you are a parent and you have purchased your 15-year-old a cell phone to use for, you know, to pick him up from football practice or something, you are not going to be able to control, to my knowledge right now, those ads coming up encouraging them to play a casino game, and target them, and start getting them playing those games online through their phones.

And the gaming industry is increasingly moving to the mobile devices, and there is no protections in place.

Senator PRYOR. I think that we all, and I heard Senator Ayotte a moment ago talk about children and, you know, just the concerns we have for children. I think age verification obviously is going to be a big challenge. It has been in other contexts on the Internet. And the easy availability of the access of Internet gaming is certainly a big concern that, you know, we have struggled with in the Subcommittee before in various contexts.

And, you know, there are technology issues about should there be some sort of blocking mechanism for parents on various devices, whether it is desktop, laptop, tablet, cell phone, you know, whatever it may be. And, you know, we talk about those sometimes in this subcommittee or there is another subcommittee in Commerce that we sometimes talk about those things. But I think that just in general, we definitely have that concern, and I think I would like to just hear more from you and, you know, work with you on this as we go forward.

And I want to thank—I am going to call you Chairman Heller today. You will be a chairman one of these days, and I just want to say I want to thank you for your leadership on this. I know this is something that is very important to you and Senator McCaskill as well. So thank you all for having this hearing, and, you know, I look forward to working with you on this issue as we go forward. Thank you.

Senator HELLER. Senator, thank you.

Senator Blumenthal?

STATEMENT OF HON. RICHARD BLUMENTHAL, U.S. SENATOR FROM CONNECTICUT

Senator BLUMENTHAL. Thank you, Chairman Heller. And I want to join—I want to thank and join in thanking you and Senator Pryor for having this hearing. I think there is a clear moral and economic imperative in acting to prevent the abuses and wrongdoing that clearly are in inherent, almost inescapable, in this form of gambling if we fail to take effective countermeasures.

And I am not sure in many areas whether they can be taken, not only because of the impact on children, but the potential dangers of fraud concerning adults, verifying means of payment, and making sure that payment is made. The resources that would be required for effective enforcement of preventive and protective measures are, in my view, staggering.

But I want to focus on one danger that perhaps has not been explored. Online gambling involves potentially huge amounts of information and data from participants, does it not?

Mr. BLUM. Senator, if I may, that is a huge problem. If I were a Russian crook, I think I would open up a casino online and steal credit card information.

Senator BLUMENTHAL. Exactly.

Mr. BLUM. Go out of business a week later. Who is to catch me?

Senator BLUMENTHAL. And you would use that credit card information——

Mr. BLUM. Instantly.

Senator BLUMENTHAL.—however you might like.

Mr. BLUM. Exactly, very quickly.

Senator BLUMENTHAL. All kinds of collateral damage.

Mr. BLUM. Of course.

Senator BLUMENTHAL. And even with the best of intentions, even an honest online gambling operator, absorbing and accumulating huge amounts of information could potentially be the victim—"victim" in very heavy quotes—of a theft of that data. Could it not happen that way?

Mr. BLUM. Absolutely.

Senator BLUMENTHAL. And do you know whether online gaming operators are taking any kind of measures against that kind of theft of their data or breach of their data? In other words, improper disclosure?

Mr. BLUM. I am sure there is a range among the people who are online operators. I am certain that the public companies or perhaps companies who have brick and mortar casinos and are regulated heavily in the states are far better at securing data than some of the other operators.

But again, there is no uniformity of regulation, and no ability to really control people from outside the jurisdiction offering products which may be utterly insecure to people inside a given jurisdiction.

Senator BLUMENTHAL. Even the most established and trusted of institutions, whether our banks or state governments, have been subject to theft or breach of data.

Mr. BLUM. Absolutely.

Senator BLUMENTHAL. So the chances are highly likely that the more online gambling there is, the more such breaches and theft there is likely to be.

Mr. BLUM. The way you have to think about online casinos is that they are, for all practical purposes, banks. They are going to have accounts. Somebody opens an account. There is a way of putting money into the account. All of that information is going to be in the hands of the casino operator, and the money can be moved, moved from one account to another, moved back to the individual. It has to be able to be moved back to the individual. So, you really are looking at creating something in a regulatory scheme that resembles what we already do for banks.

When the law was on the books, the Uniform Act, that controlled to some degree Internet gambling, it really used the banking system as a way of leveraging and controlling what these people did. So if I was an offshore guy, I could not use the banking system or credit cards to get money into my offshore accounts. When the law was undercut by that decision, the doors were opened, and now the banks simply process the money and let it all happen.

I think you have to go back to using the banks as a lever and element of control. And you also have to regulate and control these offshore enterprises, or even the—in the various states, the Internet casinos.

Senator BLUMENTHAL. My time has expired, but I would be interested in another area, which is one that was mentioned earlier concerning human trafficking. I do not know whether you have instances of online gambling associated or involved with human trafficking or similar kinds of issues. If you could provide that information, I would appreciate it.

Mr. BLUM. Well, the biggest industry on the web is pornography, and the pornography is part and parcel of all of this problem of trafficking. And there is an awful lot of money that goes flowing through the system with respect to that—with respect to pornographic websites.

I think that is an area that is worth exploring. I do not think any of these people are what we call the finest upstanding citizens of our respective states.

Senator BLUMENTHAL. And so, the two worlds merge, pornography and human trafficking.

Mr. BLUM. The same service provider I talked about in Bermuda that was offering casinos was offering online porn sites with all of the material. So, you know, it is take your pick. We will get money out of the country one way or another, and the way you do it is you just simply send the money offshore by sending it to this website, and suddenly it looks quasi-legitimate.

Senator BLUMENTHAL. Thank you. Thank you all for your excellent testimony today. Thank you.

Senator HELLER. Senator, thank you. I am going to do another quick round of questions. The Chairwoman is unable to return, so I will just have a few more questions here, and the hearing will be over.

But I want to start with you, Mr. Blum. You did a pretty good job in your earlier testimony describing probably the history of gaming in Nevada. Prior to 1967 when Senator Laxalt was elected Governor, it was the Wild West. And it was the creation of the Gaming Control Board and the creation of actually allowing brick and mortar companies to incorporate that put them under the aegis of the SEC, FBI, that they could be monitored, which was necessary. And my concern is we are back to the Wild West now.

Mr. BLUM. You are absolutely right, Senator. And that regulation, the experience of Nevada, New Jersey, are pivotal in having people understand why this has to be regulated. You guys did it, and you know why you did it.

Senator HELLER. And by the way, New Jersey did a great job, too.

Mr. BLUM. Yes.

Senator HELLER. I mean, they saw the concern, the problems, and their boards were set up also.

Mr. BLUM. And we have all been watching Boardwalk Empire, and we know the history of the people who originally wanted to control it in New Jersey.

Senator HELLER. Yes. I argued early on—in fact, we had a hearing about this on the Financial Services Committee when I was in the House, and Ways and Means Committee. And I always argued at that time that maybe a state like New Jersey or a state like Nevada ought to be doing the policing of this Internet effort. I do not think today that flies, but I thought that would have been two states anyway that were prepared. Other states are making headway, good headway—Mississippi, Missouri, and some others—in their control of their brick and mortar companies.

But I am just concerned that we have found ourselves now back to where we were prior to 1967 in that we have a free for all now of what is going on with the Internet. And the question is, and this is why you are here, as we prepare legislation, we want your input so that we can make sure that we take care of those that are most vulnerable.

Mr. BLUM. I think it has to happen on the Federal level. It has to be sophisticated. It cannot be existing agencies. So, for example, people have suggested let IRS do it. IRS is deep in its own trouble, not enough people, supposed to be implementing the health care law. It just does not have the resources and the capacity.

And the model I would see is some kind of Federal entity that does it, the finance by the people who seek licenses, and with expertise specific to this industry.

Senator HELLER. Yes. Well, I certainly do appreciate your testimony and the help it will be to formulate this piece of legislation.

I want to go to you, Mr. Grissen, and your presentation. Technology is ever changing. How do you keep in front of that? How do you keep a data breach—I mean, what keeps a person from having a picture of someone else in front of them and taking a picture of that off their iPad, sending it in? How do you stay in front of this, and how will it stop these data breaches?

Mr. GRISSEN. Sure. Great questions. You asked earlier, how do I know who it is, what their age is, and ensure that it is not a minor impersonating the father because they found their password. I would invite any of the Committee members of their staff to actually try and impersonate me. I will give you my PIN, so you can act as if you were a minor or a fraudster. The software would deny access.

So, the technology is very sophisticated. Obviously the cyber criminals continue to advance their efforts, our cyber legislation and efforts by Congress are important to bring forward the standards. It is important to be flexible in legislation to take advantage of new technologies and new innovations.

As to data breaches and security, it is important to design systems in a way that if your phone is lost, stolen, or compromised, that there is no identity information on it. That is the way proper technology is built. Encrypted using DOD type standards, so any personal information would not be available.

NIST has done some really fascinating things as part of the Nation's strategy for trusted identifies in cyberspace to separate the identity information from the records. There is an anonymity that can be pulled together to establish online trust.

Senator HELLER. I believe there is a way to do this, and I think the technology is there. We can verify that individual. I just worry about the movement of technology, the advancements of technology, and their ability to overcome any system that may be there.

Mr. Smith, I want to finish with you because I think you are the crux of the argument that we are having here, trying to help those children and those that are most vulnerable. And the concern is now you have states that are offering a lottery, instant cash prizes—instant cash prizes—on the Internet for lotteries, and the impact that clearly you see and most of us in the room see, the impact of that individual participating in that lottery, and the impact that that may or may not have, especially if you are a problem gambler, especially if you are too young.

And I want to thank you for your testimony. If you have anything to add to what you have said up to this point. I just believe preventing these kind of problems is critical, and I think it is a priority of this Congress.

Mr. SMITH. Yes, I agree with you, and you said it well.

Senator HELLER. OK. I think that is the end. My time has run out for the second round. But I want to thank everybody here, and I wanted to thank everybody also here in this audience that has taken time. This is an important subject, and my—like the Chair-

woman, my phone has rung off the hook about this particular issue, on both sides. As you can imagine, on both sides.

But it is going to take witnesses like yourselves that is going to help us formulate this. And if my staff can stay in contact and continue to receive your expertise and opinion on these particular issues, I would certainly appreciate it. But again, I want to thank you for being here and taking time from your busy schedule to help update us and for giving your testimony to this Congress. Thank you very much.

And with that, we will end this hearing.

[Whereupon, at 11:42 a.m., the hearing was adjourned.]

A P P E N D I X

NATIONAL COUNCIL ON PROBLEM GAMBLING
Washington, DC, July 12, 2013

Hon. CLAIRE MCCASKILL, Chair,
Hon. DEAN HELLER, Ranking Member,
Senate Committee on Commerce, Science, and Transportation,
Subcommittee on Consumer Protection, Product Safety, and Insurance,

Dear Senators McCaskill & Heller:

Thank you for scheduling the hearing on the Expansion of Internet Gambling and Consumer Protection. In addition to our longstanding concerns about Internet gambling and addiction I urge that you consider the burgeoning issue of social casino gaming in your review. Social casino games are gambling games played on Facebook and other social networks, including web and mobile games, that do not require users to pay to play and/or don't provide prizes of value. These games are aggressively monetized and marketed yet completely unregulated. Common social gaming features, such as high frequency, duration & speed of play, frequent but variable rewards and big early wins are all strongly associated with gambling addiction. In short, some features that make social casino games so attractive are also potentially addictive.

These games are the fastest growing segment of the gambling industry, with an estimated 170 million monthly average users and revenues of approximately $2 billion last year alone. Many of the most popular (and profitable) social casino games are operated by gambling companies. While we believe that the most social gaming is innocuous, our concerns center on three main areas:

Underage Play—While Facebook has an age limit of 13, it is extremely difficult to enforce. The majority of social casino games, sites and apps we have examined have no age limits at all. In some cases the limits are in the terms and conditions but have no enforcement mechanism. In addition, play on these gambling-like sites may condition or habituate youth to gambling, making them more likely to engage in "real money" gambling and/or develop gambling problems. We know from decades of research that the earlier kids start to gamble the more likely they are to have problems. Pathological gamblers in treatment report on average they began gambling seriously for money at age 12. Also, many social gaming sites use animation and/or cartoon images that may appeal to younger users. The Chair of the U.K Gambling Commission reported earlier this year that nearly 600,000 young people claimed that they had either gambled or played free games online in Britain in the past week.

Fairness—While social casino gambling sites use names, images and themes related to gambling, there are important but often hidden differences. One is that most sites use "adaptive" or "reflexive" algorithms and game mechanics designed to increase the time spent playing the game by modifying the results so that the longer you play the more likely you are to win. This obviously encourages play, but it may be problematic when users are also encouraged to pay for their chips or coins in order to progress within the game. It also may create erroneous expectations for winning that, when the user switches to "real money" gambling—often hosted or operated by the same company—that are extremely dangerous as the longer you play the more likely you are to lose since the odds are now against the user. There is little consumer protection or disclosure in general in this space. Social casino games are not regulated by either state gaming commissions or by hosts like Facebook or Internet service providers. While NCPG has proposed a voluntary code of conduct, no advertising or responsible gaming standards have been adopted by the industry.

Gambling Addiction—The criteria for gambling addiction includes gambling with increasing amounts of money to achieve more excitement, attempts to cut back time and money spent, preoccupation, playing when feeling distressed (*e.g.,* helpless, guilty, anxious, depressed) to relieve or escape these feelings. Most importantly, problem gamblers report that the action is the high they seek, it is the betting and

amount of risk that is exciting and addicting, not how much they win or lose. Indeed, every study of Internet gambling addiction has found a higher rate of problem gamblers among those who gamble online. Even if social casino gamblers rate isn't elevated, the general public prevalence rate of 1 percent means that approximately 1.7 million monthly social casino users are likely to suffer from gambling addiction. At-risk gamblers and current problem gamblers may be attracted by or to social casino gaming.

We have broader concerns about online gambling and consumer protection. For example, studies have found that some Internet casino sites provide inflated payout rates when gamblers play on the slot machine demo games. One published study found 40 percent of sites surveyed provided inflated payout rates (over 100 percent) in the demo session. But these unrealistic high rates were not maintained when playing for real money. In addition, some sites used marketing strategies reinforcing false beliefs about the notion of chance and randomness. None of the state Internet gambling regulations introduced to date fully incorporate our Internet Responsible Gambling Standards, a compilation of best practices from regulators around the world to help protect Internet gamblers. Nor has there been sufficient state funding for problem gambling programs—states and non-profits spend approximately $60 million per year to fight gambling addiction, approximately 1 percent of the $6 billion in annual social cost, and less than one-tenth of one percent of the 2012 legal gambling revenue of $95 billion. As a result, most states do not have adequate public health or consumer protection programs in place to address current gambling problems, let alone expanded Internet gambling.

I attach a copy of my testimony at the most recent House hearing on Internet gambling that highlights these larger issues, including the lack of any Federal funds or staff for national programs or assistance to state health agencies to prevent and treat gambling addiction. Now that 48 states have some form of legalized gambling, and 75 percent of adults (and children aged 13–17) report having gambled in the past year, it is very timely to look at the broad public health and consumer protection aspects of this activity, especially as technology encourages and regulation allows gambling to flourish online and increasingly via social networks.

The National Council on Problem Gambling is the national advocate for programs and services to assist problem gamblers and their families. NCPG does not take a position for or against legalized gambling. We were founded in 1972 and our 41-year history of independence and neutrality makes the National Council the most credible voice on gambling issues. The National Council has 37 state Affiliate chapters, including in Missouri and Nevada. NCPG is a 501(c)(3) not-for-profit charitable corporation and does not accept any restrictions on contributions.

The expansion of Internet gambling, including social casinos gambling, includes new risks for consumers, new responsibilities for state governments, regulators and operators, and possibly new opportunities for consumer protections. Please feel free to contact us with any questions.

Sincerely,

KEITH WHYTE,
Executive Director.

RESPONSE TO WRITTEN QUESTION SUBMITTED BY HON. AMY KLOBUCHAR TO CHUCK CANTERBURY

Question. Enforcement of our laws, whether state or federal, is important to the protection of consumers and our national security. Your members enforce laws aimed at keeping consumers safe in interstate markets like gambling. Can you expand on how you work with law enforcement entities at various levels of government and across jurisdictions? Are there ways these relationships can be improved?

Answer. I appreciate the opportunity to respond because this is an important question and it demonstrates the thrust of my testimony before the Subcommittee, which is that Congress must act to build a Federal regulatory framework to facilitate protections for our citizens and a means by which law enforcement can cooperate to shut down bad actors. Without such a framework, law enforcement agencies are unable to coordinate effectively.

The first challenge law enforcement would have is to identify if there was a crime committed and, if so, in what jurisdiction the crime occurred. For example, if an Internet user places a bet or buys a product from his home in one state and money from his account is sent from an Internet server physically located in another state to an off-shore operator who accepts the money and then disappears without placing or paying the wager or sending the product to the buyer, in which jurisdiction has the crime been committed? The state where the user placed an illegal sports bet?

The jurisdiction from which the money transfer was authorized? Or did the crime occur offshore when the operator denied or withheld the payment or product? Right now, without any coherent Federal strategy in place, these questions have to be answered by local and state law enforcement agencies. It becomes a very real question of resource allocation: can the agency spare the manpower to sort this out and coordinate with other jurisdictions, perhaps including those overseas? I suspect in many cases, the answer to this will be no. State and local agencies must prioritize their resources to respond to crime which occur in their jurisdiction. Unless we are looking at a large scale money laundering operation and we have the full cooperation of Federal law enforcement agencies, I think it is doubtful in most cases that a smaller agency will be able to investigate a complaint like the one I have described.

In cases where there is suspicion of large scale criminal activity, the Federal Government must be involved. Consider, for example, how the Federal Government was able to bring charges against 11 defendants under both the Unlawful Internet Gambling Enforcement Act (UIGEA) and the Illegal Gambling Business Act (IGBA). The latter statute was adopted by Congress in 1970 in an effort to attack the profits of organized crime. Apart from the individual making the wager, the statute allows any person that plays a role in the business or organization of conducting a gambling business to be charged with violating or conspiring to violate the Act. A key component to this law, however, is that there must be a *State* statute prohibiting the activity, which then would allow the Federal Government to investigate and prosecute the case. The indictments were brought using the State of New York, which defines gambling as taking place based on the location of the bettor. In other states, bettors may be able to call-in their wagers to an offshore bookmaker and not be in violation of state law, thus precluding the Federal Government from using the IGBA to go after these criminal enterprises. Obviously, this is not a very effective national strategy.

Compounding this difficulty, several states have approved and many more states are actively considering proposals that would legalize various forms of Internet gambling, such as poker, lotteries, and casino games, all of which are no longer deemed unlawful by the Wire Act. Such state-authorized and promoted wagering, in conjunction with rampant gambling on offshore sites out of the reach of Federal and state prosecutors, will undoubtedly result in a dramatic increase in Internet gambling in the United States. Patchwork state and tribal regulations could also spark a regulatory race to the bottom without Federal standards and coordination with Federal law enforcement.

I hope this answers our question fully and I want to assure you that the more than 330,000 members of the Fraternal Order of Police are eager to work with you and other Members of Congress to address this issue. If I can be of any further assistance or provide you with additional information, please do not hesitate to contact me or Executive Director Jim Pasco in my Washington office.

RESPONSE TO WRITTEN QUESTION SUBMITTED BY HON. AMY KLOBUCHAR TO JACK A. BLUM, ESQ.

Question. The idea of expanding states' authority on Internet gambling raises concerns among some of the brick and mortar gaming operations. Can you discuss how you expect states to work with existing operations and how we can make sure that any discrimination or inconsistencies in rules or regulations are addressed?

Answer. I do not believe that Internet gambling can be successfully regulated by the states. The states do not have the resources to develop agencies with the capacity to deal with the problem. Regulation has to come at the Federal level. If the brink and mortar facilities are regulated at the state level I assume the Federal regulator would coordinate with the state agencies. That would eliminate discrimination and inconsistencies.

RESPONSE TO WRITTEN QUESTION SUBMITTED BY HON. KELLY AYOTTE TO CHUCK CANTERBURY

Question. As you know, nearly 2 years ago the Department of Justice rolled back 50 years of established law by stating the Wire Act only applies to online sports betting. By limiting the scope of gaming operations enforceable under the Act, how has this affected your ability to crack down on illegal operations? When states are allowed to sanction various online gaming ventures within their borders, what additional challenges are faced by law enforcement? Does this make it easier or harder to protect consumers?

If online gambling continues to expand freely into the states with no or limited Federal regulators, do you have any confidence in state agencies cracking down on malicious actors? Is it realistic to expect a state to slap the hand of one of its agencies which is raising millions of dollars in revenue each year? Would you expect it to be common play for regulators to look the other way on age verification and authentication? What is their incentive to strictly enforce the laws?

As we address this issue, we must make sure there are meaningful regulations where states can opt out. We must make sure that we address child protections, addictions, anti-terrorist funding, money laundering and drug trafficking. I am concerned after Attorney General Holder upended the Wire Act and UGIEA, it made it easier for revenue-starved states to take advantage of citizens in other states. How do we make sure the integrity of the borders of New Hampshire are protected? Does a state-by-state approach make the most amount of sense? How do we maintain any control over payment systems?

Answer. I appreciate the opportunity to respond because these are important questions which go to the heart of my testimony before the Subcommittee: It is Congress, not the states acting independently, that must act to build a Federal regulatory framework to facilitate protections for minors and other at-risk citizens, as well as a means by which law enforcement can shut down bad actors. States working without a national framework will be totally ineffective.

Let me begin by stating that the Memorandum of Opinion issued by the Assistant U.S. Attorney General in the Office of Legal Policy in December 2011 was not the start of law enforcement problems related to Internet gambling. The Federal law has never caught up with the technology, so the existing ambiguities in the application of Federal laws, most prominently the Wire Act, to Internet gambling impeded law enforcement's ability to combat illegal activity at the Federal level. Existing gambling enforcement tools did lead to Federal indictments of several major Internet gambling operators in the spring and the fall of 2011, but almost all of the charges were based on money laundering and bank fraud laws. None of these operators have been charged with offenses that directly dealt with Internet gambling activity that is offered by a myriad of offshore Internet sites to U.S. citizens. In fact, as I made clear in my testimony, the Federal charges brought against these defendants under the Illegal Gambling Business Act were dependent on state law.

Every expert agrees that millions of Americans continue to gamble on the Internet even though such gambling is illegal, unregulated, and offers no consumer protections. Internet gambling is run by offshore operators, some of which operate from regulated foreign jurisdictions, but many of which operate from small Caribbean countries that do little to regulate the gambling and do nothing to protect consumers and minors. These operators also often offer online sports betting, as well as casino-banked games, such as slots and roulette.

Prior to the opinion released by the U.S. Department of Justice, many states were considering legalizing and promoting intrastate Internet gambling to generate revenue. In the wake of the opinion, several states have approved and many more states are actively considering proposals that would legalize various forms of Internet gambling, such as poker, lotteries, and casino games. Such state-authorized and state-promoted wagering, in conjunction with rampant gambling on offshore sites that are beyond the reach of Federal and State prosecutors, will undoubtedly result in a dramatic increase in Internet gambling in the United States. The FOP is concerned that, absent Federal standards, a patchwork of laws could result in a regulatory race to the bottom as states and sovereign tribes compete for gambling revenues.

The law enforcement and consumer safety risks associated with Internet gambling, particularly unregulated foreign Internet gambling, are well-known and were well covered at the recent hearing. It is the position of the FOP that Congress must update the Wire Act of 1961, the Illegal Gambling Business Act of 1970, and the Unlawful Internet Gambling Enforcement Act of 2006 to ensure that they clearly apply to modern technologies and to all forms of prohibited Internet gambling. Legislation should strengthen enforcement by providing tools, such as a "good actors" list, to crack down on unlicensed operators, thereby empowering law enforcement to work with financial institutions in shutting down and illegal activity, as well as stiffen penalties against illegal operators.

On the issue of permitted Internet gambling, as I stated in my testimony, the FOP is not advocating for any expansion in defining what online gaming activity is deemed unlawful. This was the position we took when we supported UIGEA and it is the position we still hold.

RESPONSE TO WRITTEN QUESTIONS SUBMITTED BY HON. KELLY AYOTTE TO MATT SMITH

Question 1. In your testimony, you indicate that state lotteries were given a gift when the Department of Justice reversed its long-standing view that all Internet gambling was unlawful. In the Internet age, every smartphone could become a slot machine. Please expound on your testimony to explain your concerns about the explosion of Internet gambling which many contend is right around the corner.

Answer. Senator Ayotte expressed concern about her children's ability to play games on mobile devices, a concern we share. It is our children that will be highly targeted by online Internet gambling proprietors. As I stated in my testimony, "Ninety-three percent (93%) of teens age 12–17 utilize the Internet and 97 percent of teens of the same age participate in some form of online gaming making them attractive targets for gambling marketing as well as illegal and fraudulent operators." This makes Internet gambling not something containable to adults or inside state boundaries when anyone with a mobile device can travel with their own pocket casino. Everyday younger and younger children are being given devices on their parents' accounts. Cleaver marketers are going to find ways around safeguards and technology to reach the purchasing prowess of America's youth. And, as was discussed during the hearing, there is a very frightening possibility of human trafficking by international criminal enterprises who will once again engage in online gambling sites. We believe the state lotteries that pushed for the Department of Justice's memo out of a desire for sources of revenue are ignoring who will actually be marketed to and become the victims of the forthcoming expansion of on-line gambling.

Question 2. I recently read a statistic that approximately 2 million Americans suffer from gambling problems and addictions and about 1 percent of the worldwide population (according to the National Council on Problem Gambling). With the prevalence of unregulated offshore sites, it would seem that the United States finds itself in the unfortunate position of incurring all the social costs of online gambling while having no control over the sites that serve U.S. citizens. In your capacity as President of the Catholic Advocate, can you talk about your experience working with those who suffer from addictions?

Answer. While directly working with those who suffer from addictions is outside our mission, we are concerned about the cost and impact on the family that comes with addiction as it relates to public policy. We believe experts in addiction science should be consulted about the consequences are part of this discussion. Gambling addiction affects personal relationships. Divorce, child abuse and suicide are all too common in homes where pathological gambling is present. One example in the United States, a report by the National Council on Problem Gambling mentioned in the question found approximately 20 percent of pathological gamblers attempt suicide. The Council also said suicide rates among pathological gamblers are higher than any other addictive disorder. We are concerned, at the state level, there has been a short-sided examination about the true costs associated with expanding gambling into every home in America. The debates at the state level surround increased revenue from Internet gambling, but very few are expressing concern about the aftermath. As a result, when the true costs begin to reveal themselves down the road, every level of government will be burdened with increased spending on addition and other related social services programs.

RESPONSE TO WRITTEN QUESTIONS SUBMITTED BY HON. KELLY AYOTTE TO JACK A. BLUM, ESQ.

Question 1. The U.S. Treasury Department has several comprehensive international anti-money laundering programs that work 24/7, 365 days a year in an attempt to safeguard our international and domestic finance systems. Criminals from the beginning have laundered the proceeds of their illegal activity through a number of legitimate and illegitimate means. From my experience as Attorney General, I would argue that this is an area where state and local law enforcement need the Federal Government's assistance. First, do you agree with this, and second, are you concerned that unregulated offshore gambling sites may be used for money laundering purposes? In your estimation, what can Congress do to enhance our anti-money laundering capabilities?

Answer. Money laundering controls have to operate at the Federal level to be effective. State law enforcement authorities have other priorities and concerns and lack the necessary resources. With exception of New York, most lack the jurisdiction and expertise to conduct a major money laundering investigation. New York is the

exception because as a banking center most fund movements touch the New York banks and the New York Fed. Further, some states lack robust laws aimed at money laundering.

I am quite concerned about unregulated offshore gaming sites being used as a vehicle for money laundering. A casino—offshore or onshore—is very much like a bank. Customers have accounts. They deposit money to gamble, winnings and losses are either added to or taken from the account and the gambler can ask for the funds in the account to be returned. Of necessity the casino accounts will be encrypted. A casino controlled by gangsters could easily be used to move money either into or out of the country disguised a gambling fund or gambling winning. The corrupt casino operator could easily transfer funds from one account to another thus disguising the connection between the origin and the destination of the funds.

All online casinos should be federally licensed and federally regulated. There should be severe penalties for U.S. persons gambling through unlicensed casinos. Banks and credit card companies should require a showing that the casino has a license before they can transmit funds to or from a casino. Finally all casinos are subject to the Bank Secrecy Act and the provisions of the Patriot act. They are obligated to identify their customers and screen transactions for suspicious activity. This obligation must be enforced either by gaming regulators or by the existing regulatory agencies.

The two most important steps would be to increase funding for regulators and prosecutors and the push prosecutors to send revoke banking licenses when banks are caught in the act. At the moment the Justice Department uses "deferred prosecution agreements" to avoid threatening a bank's license.

Question 2. Mr. Blum, when there are 50 jurisdictions instead of 1 jurisdiction, how has this opened up the flood gates for corruption, money laundering and additional crime?

Answer. Any crook seeking to avoid state prosecution will use multiple jurisdictions to run their operations. The casino's incorporation will be in one state, the server running the software in another, the operator and manager in a third and the banking relationships in a fourth or a fifth. Because there is little corporate transparency and because the practical problems of enforcing laws across state lines are immense, organized crime will have a field day.

Question 3. What means do states have to monitor large scale laundering of capital by other countries, terrorist networks, or international crime syndicates?

Answer. With the exception of New York, states are powerless to operate in the international arena. They lack the budget, the expertise, the ability to gather evidence and many cannot make use of the international mutual legal assistance agreements. For example, the Cayman Islands argue that its agreement with the U.S. is limited to the Federal Government.

RESPONSE TO WRITTEN QUESTION SUBMITTED BY HON. KELLY AYOTTE TO THOMAS A. GRISSEN

Question. As a former prosecutor and Attorney General, I have built a career enforcing our laws and going after those attempting to circumvent our rules. In your testimony, you argue that the tools we have in place are inadequate. I wholeheartedly agree. When Attorney General Holder opened the flood gates to online gambling, he made it infinitely more difficult to target corruption, money laundering and fraud. While I applaud your commitment to creating software that improves identity assurance and verification, what assurances can you give this committee that online verification is foolproof? Convenient stores claim they spend millions of dollars training their clerks to identify fraudulent actors. How would you compare the ability of your software to identify a fraudulent actor verse a person in a store? Is it easier to get around this verification online? What more needs to be done to verify age and geolocation online?

The Federal Government faces serious enforcement challenges in this area. What assurances does a state which opposes Internet gambling have that sites licensed in other states will be 100 percent effective in preventing play by residents of states where online gambling is illegal?

Answer. Thank you for [your] thoughtful questions about the ability of state-of-the-art Ecommerce trust verification systems and technology to assure and verify identity. I am confident that the fuller description of these systems and technology provided below will leave [you] no doubt about the relative efficacy of Ecommerce solutions to customer identification versus those deployed in the convenience store industry.

I describe below a generic online gambling customer identification solution based on current technologies employed in other sensitive Ecommerce sectors. The technology most certainly exists for such a system in the online gambling space, but as I indicated at the Hearing, I am unaware of any state using or requiring the technologies I describe that might be the underpinnings of any Federal standards regarding the responsible provision of Internet gambling.

Identity Verification and Internet Gambling

Critical to an effective regulatory process that assures and verifies customer identity, are strict regulatory requirements mandating a series of rigorous player identification processes prior to establishing a new account to play and verifying identity at time of play (log-in). These regulatory requirements and processes would, beyond a doubt, offer much better safeguards against a number of customer identification risks (*e.g.,* underage gambling) than exist in the brick and mortar industry, given the fact that the identities of adults can be validated through real-time automated crosschecks of existing databases and biometrics that are not utilized in brick and mortar gambling establishments.

An acceptable solution would be a step-wise Know Your Customer protocol like the one described below that builds a profile of the prospective online gambling customer. That is, age verification, identity verification, geo-location and cross checking against databases of unwanted persons are components in an integrated process. Operators and regulators alike would then have a level of comfort that each prospective customer is who s/he say s/he is, is of legal age, is located in a jurisdiction where the activity is legal and is not otherwise barred from participation. Moreover, the system would provide the operator and regulator a full and complete audit trail addressing these issues as well as other issues focused on consumer protection, fraud prevention and compliance with anti-money laundering and other laws.

Player Registration—The first step involves identifying a prospective customer's IP address and verifying that the customer is physically located in a jurisdiction that permits online gambling. Assuming that the customer's geo-location is verified and appropriate, an automated callback would be made to the landline telephone linked to the address provided by the customer during the registration process, using a reverse lookup of phone records. The customer is asked during the callback to input, on the telephone type pad, a verification number that is visible on the customer's computer screen. Successful completion of this process mitigates that the customer is residing at the address provided and that the person is indeed seeking to open the account.

If the process is successful, personal identification information provided by the customer is then cross-matched against various government-maintained databases of undesirable individuals. Individuals on such lists would not be permitted to open an account.

A further step would leverage the ability to triangulate the location of a user's IP address with the location of a user's mobile device through a SMS (short messaging service—commonly known as a "text message") coupled with "global positioning technology" (GPS). Using one of many technology providers, a SMS text is sent to the user. The user would then be required to click a confirmation link with their mobile device. In addition to triangulating the player's exact location to within five to ten meters, this step validates that the mobile number entered is indeed the number of the player. If the check is inconsistent with either the IP address information or other location data obtained from the player or if the player is located in a jurisdiction that does not authorize online gambling, registration will be suspended.

In a well-regulated online gambling regime, all operators would be required to verify the identities, locations, and ages of their customers. Among other things, prospective customers would be required to provide data such as their name, address, date of birth, driver's license number, social security number and credit/debit card information.

Of course, if a prospective customer volunteers a date of birth indicating that the customer is underage, that customer would be barred from opening an account.

If the date of birth provided does indicate a customer is "of age", then the operator of an online gambling service would use one or more independent data service companies (such as those currently in use to verify age and identity online for shipment of alcohol or tobacco) to test whether the name and address match the date of birth provided. These independent data service companies use a variety of specialized databases, (including credit data, driver's license and voter information) to cross-reference and verify the identity and age of the individual.

A failure to verify either age or identity would mean that the customer may not open an account. The customer may, however, have the option of providing physical

copies of identifying records (such as a driver's license or passport) for further review by the operator.

I would add that in a well regulated environment, the use of a credit card alone for age verification would be prohibited as a source of verification, as the use of credit cards for age verification is a violation of most credit card company terms and conditions. Also, potential improper access to others' credit cards by minors prohibits this as an effective control.

Even if a customer's age and identity successfully pass each of the steps above, the verification process does not end there. The social security number provided by the customer would be used to generate a list of personalized challenge questions (concerning, for example, previous cars registered, previous addresses, etc.), all of which the customer would have to answer correctly before an account is opened. Again, the goal is to ensure that the customer is who s/he says s/he is and of the age represented.

After an operator has performed the challenge questions and confirmed that a person is who they say they are, at registration, each player will be mandated to register with biometric confirmation—facial and/or voice recognition, as I demonstrated in the Hearing. This requirement will preclude anyone from

assuming someone else's identity on subsequent log ins; all but eliminating the issues some have raised with minors using their parents' or others' credit cards and also providing additional protections on fraudulent transactions by third parties.

Only if all of these steps are successfully completed could the operator permit a customer to open an account in a well regulated environment.

While identification of the customer when registering for play is accomplished by cross-matching government issued ID and other information customers supply using the specialized databases and biometrics described above, there are a number of additional tools available to operators and regulators. For example, a confirmation letter might be sent subsequent to the opening of an account to the address listed on government issued identification. This process would be similar to that used when a PIN number is changed with an airline, or bank, that serves as a notification that an account has been opened.

Log-in—Verification of a player's identity would not end at the player/account registration process. On log-in, the player would either use voice recognition and/or facial recognition through their mobile device as part of the log-in process. This will not only accurately pinpoint the location of the player to within meters of their location (verifying whether a player is or is not in a jurisdiction that permits online poker play) but it will also assure that the player is the original player—the same adult—who created the account.

Cash-out—Cash-out also provides an opportunity to verify a customer's identity. After a request by a customer to cash-out, the operator would send a request to the player's mobile device (separate and apart from their computer) in order to validate the player's identity either through voice or facial recognition. At the same time, through geo-location technology, the location of the player will be triangulated and this information is stored for full audit use by the operator and regulator. As an additional protection, players could also be required to submit a valid photo ID as well as proof of residency at the time of their 1st cash-out.

The best strategy to achieve reliable and secure geo-location is a multi-pronged approach that incorporates data from various sources.

Beginning with the user's first interaction with the system—registration: personal information (name, driver's license #, address, phone #, etc.) is collected and stored, along with his/her IP address, and a "Device ID" for the computer (*e.g.,* laptop).

This data is then verified with a service that can score the identity's veracity and fraud profile (including age verification, address velocity calculation, connections to previous data used in fraud, etc. . .).

IdentityX enrollment is also a part of this registration process, which begins collecting GPS information and the IP addresses used by the mobile device.

All of this data is then used to determine the user's location at a given time. For example:

- The user's personal information scores highly for legitimacy, and low for fraud.
- The user's IP address is used, in combination with personal information, to estimate the user's location to an allowable area.
- The user's GPS coordinates are consistent with the above data and in the allowable area.
- User is then allowed access.

Human reviewers can be employed only in cases where the system has flagged the user as having an unusually high risk/fraud profile and/or GPS and IP indicates the user is outside of bounds.

The Nexus Between Regulation and Technology

It's important to remember that regulators control the thresholds for accepting, rejecting or requiring further information concerning customer identity verification, and can impose additional requirements that can further mitigate/eliminate relevant risks. Regulations can establish requirements based on the levels of assurance that are necessary to allow a customer to gamble, thereby fine-tuning the balance between failing to detect an underage individual and rejecting a player who is of the legal age. In other words, regulatory requirements can "turn up the dial" with respect to unknown or suspicious entrants to a site, which has the effect of minimizing the potential harm if a customer falls into a grey area. States should be free to establish policies and procedures that exceed mandated Federal standards and protections. By implementing a solution that embraces flexibility, through the union of complementary technologies, regulators are empowered to effectively tune this dial based on the needs of the public.

I would like to thank Senator Ayotte for providing me the opportunity to elaborate on the nuts-and-bolts of the technologies and systems that I demonstrated at the hearing. I appreciate and share her concerns about the potential for fraud, corruption, and money laundering associated with unregulated or poorly regulated online gaming and other forms of Ecommerce. I am happy to answer any additional questions or otherwise provide assistance.

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