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The Regulation of Internet Gambling in the United States: It's Time for the Federal Government to Deal the Cards

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The Regulation of Internet Gambling in the United States: It's Time for the Federal Government to Deal the Cards

By Benjamin Miller*

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I. INTRODUCTION

Over the last decade, Internet gambling, as an industry,¹ has been on a roller coaster ride in terms growth and regulation; the industry has experienced extreme peaks and valleys in its success in the United States.² After what seemed like a crippling defeat in the Legislature,³ the legality of Internet gambling has changed in such a way that seemingly will result in widespread growth and legalization within the states, with state laws continually testing the boundaries of current federal Internet gambling laws.⁴ Government regulation of this recent expansion is currently limited to state law enacted within the framework of the vague, overarching federal gambling law, but the need for some specific federal regulation of Internet gambling has been recognized and attempted.⁵

This comment will provide an overview of the history of gambling laws and regulations in the United States to establish a

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¹ For players, “the industry” has evolved from what most would consider a recreational activity into a profession, especially for Internet poker players. *See Biggest Poker Winners, HIGH STAKES DATABASE*, <http://www.highstakesdb.com/poker-players.aspx?sortby=winners> (last visited Aug. 1, 2014) (showing professional poker players with the most total profit playing Internet poker).

² *See infra* Part III.

³ Internet poker specifically has suffered defeats at the hands of the federal government due to enforcement of the Unlawful Internet Gambling Enforcement Act of 2006 against online poker players in 2009 and the largest online poker sites in 2011. *See infra* Part III.C–D. As a result, players’ accounts were frozen and poker sites exited the United States market. *See infra* Part III.C.

⁴ *See infra* Part IV.

⁵ *See* Internet Gambling Regulation, Enforcement, and Consumer Protection Act of 2013, H.R. 2282, 113th Cong. § 101(a)(5) (2013) (as referred to the H. Subcomm. on Crime, Terrorism, Homeland Sec., and Investigations, July 15, 2013), *available at* <http://www.gpo.gov/fdsys/pkg/BILLS-113hr2282ih/pdf/BILLS-113hr2282ih.pdf> (recognizing the need for federal enforcement because purely state regulation of Internet gambling, including consumer safeguards, varies widely between and among states, and states may not be able to adequately meet the challenges inherent in enforcing Internet gambling restrictions within their borders, especially against sophisticated out-of-state operators).

framework for the analysis of regulation of Internet gambling. Next, this comment will discuss the current state of the law regarding Internet gambling in the United States and the effects of recent legal developments in the industry. This comment will expound on state action in the realm of Internet gambling, including proposed legislation, the expansion of state gambling commissions, and successfully enacted legislation. Finally, this comment will analyze the implications of state actions and how they relate and contribute to federal proposals for national regulation of Internet gambling, including the establishment of a federal gambling commission.⁶

II. HISTORICAL BACKGROUND

A basic understanding of the history of gambling laws in the United States provides an important perspective in analyzing the many arguments for and against recent changes in Internet gambling laws, as well as the roles of gambling commissions in enforcing such laws. This section illustrates the history of gambling laws in the United States and the rationale behind them. Many of the same concerns that have applied throughout history are considered in current Internet gambling regulations. Specifically, some of the most important considerations that lawmakers must balance in regards to gambling laws are: (1) the revenues that gambling generates, (2) the issues of controlling cheating and corruption within gambling frameworks, and (3) the social concerns that legalized gambling promotes.⁷ There are many types of “games” that fall within the

⁶ For a detailed, comprehensive “best practices” analysis of the elements that compose an Internet gambling regulatory scheme (such as licensing, taxation, financial transactions, technical compliance, fraud or cheating, age verification, and more), see ANTHONY CABOT & NGAI PINDELL, *REGULATING INTERNET GAMING: CHALLENGES AND OPPORTUNITIES* (Anthony Cabot & Ngai Pindell eds., 2013).

⁷ See I. NELSON ROSE, *GAMBLING AND THE LAW* 29–30 (Gambling Times Inc., 1986) (“Why regulate at all? The standard reasons given are to ensure competency of the operators while keeping organized crime out. Perhaps more important are the twin issues of money and image. . . . And legal gambling is always subject to attack from outsiders; like alcohol, the industry has to be extremely careful about its reputation for causing harm or it can find itself easily outlawed again.”); see also JOHN LYMAN MASON & MICHAEL NELSON, *GOVERNING GAMBLING* 83 (The Century Found. Press, 2001) (“The most widely discussed problems with Internet

umbrella of the term “gambling,” and technological innovations like the Internet have only increased the ways and means by which gambling can occur.⁸ This discussion is especially relevant for the topic of Internet gambling. History shows that the technology is usually ahead of the regulation, and there is no clearer example of this than Internet gambling law.⁹

Gambling in the United States started in the Colonial era, primarily in the form of lotteries.¹⁰ Early gambling posed many challenges in terms of cheating and corruption, but the revenue was always the driving factor for those in the lottery business.¹¹ Each of the thirteen original colonies started lotteries to raise revenues, and this practice continued within the states after the United States became an independent nation.¹² However, these early nineteenth century lotteries often struggled with corruption, in part because of the lack of adequate oversight.¹³ Public outcry over corruption and the regarded immorality of gambling led the majority of states to prohibit lotteries by the mid-1800s.¹⁴ Predictably, this led to the establishment of many illegal lotteries.¹⁵ Instead of establishing a regulatory scheme that could effectively extinguish corruption and other problems with state lotteries, states prohibited them

gambling fall into three categories: gambling disorders, especially among young people; crime; and burdens on government.”).

⁸ See MASON & NELSON, *supra* note 7, at 82 (“Technological advances continue to make it faster and easier to download from gambling websites the software needed to play games and place bets, and the speed of the games . . . is increasing.”).

⁹ See *infra* Part III. This section explicates federal statutes regulating Internet gambling enacted prior to the advent of the Internet.

¹⁰ CHARLES T. CLOTFELTER & PHILIP J. COOK, *SELLING HOPE: STATE LOTTERIES IN AMERICA* 20 (Cambridge, MA: Harvard Univ. Press, 1989).

¹¹ *Id.*

¹² Roger Dunstan, *History of Gambling in the United States II-1*, GAMBLING IN CALIFORNIA (Jan. 1997), <http://www.library.ca.gov/crb/97/03/Chapt2.html>.

¹³ See *id.* (“lottery passed by Congress in 1823 for the beautification of Washington D.C.” never paid out); see also CLOTFELTER & COOK, *supra* note 10, at 37.

¹⁴ See Dunstan, *supra* note 12 (“By 1840, most states had banned lotteries. By 1860, only Delaware, Missouri, and Kentucky still allowed state-authorized lotteries.”).

¹⁵ See *id.*

altogether.¹⁶ This pattern is one that recurs time and again in United States gambling laws, and is particularly apparent in the relatively recent laws specific to Internet gambling.¹⁷

Laws banning gambling faded quickly when the government's outlook dramatically changed after the economic devastation of the Great Depression.¹⁸ As states began to rediscover the value of gambling for generating revenue—especially during periods when taxes were heavily opposed—state lotteries returned and some states legalized casino gambling.¹⁹ Soon after the return of state lotteries, Congress began to enact federal laws applicable to gambling on a broader scope, many of which apply to Internet gambling.²⁰

III. FEDERAL INTERNET GAMBLING LAW

In order to fully comprehend the current federal law on the topic of gambling, it is essential to understand the relationship between state and federal law. Under the Tenth Amendment of the Constitution, states' police powers give them the power to regulate gambling within their respective state jurisdictions.²¹ States have

¹⁶ *See id.*

¹⁷ *See Dunstan, supra note 12; see generally infra* Part III. This section will illustrate federal laws banning Internet gambling in response to the same societal concerns of corruption and immorality, as well as the forums commonly utilized to participate in illegal Internet gambling.

¹⁸ *See Dunstan, supra note 12* (“Legalized gambling was looked upon as a way to stimulate the economy. . . . Bingo was legal in 11 states by the 1950s During the 1930s, 21 states brought back racetracks.”).

¹⁹ *Id.* Two years after the stock market crash in 1929, Nevada became the first state to legalize casino gambling, with New Jersey following suit in 1978.

²⁰ *See generally* I. Nelson Rose & Rebecca Bolin, *Game on for Internet Gambling: With Federal Approval, States Line Up to Place Their Bets*, 45 CONN. L. REV. 653, 659 (2012) (“Today’s federal laws governing Internet gambling are a patchwork that reflects disparate treatment for different types of gaming, uncertainty about the laws’ application for particular types of technology and gaming, and questionable federal interference into state gambling policies.”).

²¹ *See* U.S. CONST. amend. X (“The powers not delegated to the United States by the Constitution, nor prohibited by it to the States, are reserved to the States respectively, or to the people.”); *Ah Sin v. Wittman*, 198 U.S. 500, 505–06 (1905) (“The suppression of gambling is concededly within the police powers of a state, and legislation prohibiting it, or acts which may tend to or facilitate it, will not be interfered with by the court”); *Johnson v. Collins Entm’t Co.*, 199 F.3d 710,

wide latitude in exercising this regulation, and the spectrum ranges from Nevada, which offers the gambling oasis of Las Vegas, to Utah, which is one of only two states in the United States that has not legalized some form of gambling.²² As for whether an activity constitutes gambling, most jurisdictions apply the “dominant factor” test, which evaluates whether chance rather than skill is the dominant factor in controlling the award.²³ While states have the power to regulate gambling policy within their borders, the federal government may step in if gambling activity crosses state or national borders through its power under the Commerce Clause of the Constitution.²⁴ Using this power, Congress has enacted several statutes that have been applied to the regulation of Internet gambling, and the following subsections will discuss the most relevant of the statutes in detail. These statutes are often unclear and, in some ways, seem to contradict each other.

A. *The Wire Act*

Enacted in 1961, The Wire Act²⁵ is the oldest piece of federal legislation analyzed in this section. In section (a), it provides:

Whoever being engaged in the business of betting or wagering knowingly uses a wire communication facility for the transmission in interstate or foreign commerce of bets or wagers or information assisting

720 (4th Cir. 1999) (“The regulation of gambling enterprises lies at the heart of the state’s police power.”).

²² See UTAH CRIM. CODE §§ 76-10-1101 to 1109 (1953) (statutes prohibiting gambling). The second state without legalized gambling is Hawaii. HAW. REV. STAT. §§ 712-1220 to 1231 (1973). Hawaii’s state law makes gambling a misdemeanor and defines gambling as when a person “stakes or risks something of value upon the outcome of a contest of chance.” *Id.*

²³ See *State v. Dahlk*, 111 Wis. 2d 287, 296 (Ct. App. 1983) (finding that “[m]ost jurisdictions apply the ‘dominant factor’ test.”). For a more thorough discussion of the dominant factor test, see James Romoser, *Unstacking the Deck: The Legalization of Online Poker*, 50 AM. CRIM. L. REV. 519 (2013) at Section II Skill Versus Luck: Poker at the State Level.

²⁴ U.S. CONST. art. I, § 8, cl. 3 (“To regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes.”).

²⁵ 18 U.S.C. § 1084 (2012).

in the placing of bets or wagers on any sporting event or contest, or for the transmission of a wire communication which entitles the recipient to receive money or credit as a result of bets or wagers, or for information assisting in the placing of bets or wagers, shall be fined under this title or imprisoned not more than two years, or both.²⁶

It was originally enacted to combat the then-rampant organized crime activity of sports betting via telegraph.²⁷ The Wire Act essentially prohibits three types of “wire” transmissions in interstate or foreign commerce: (1) bets, wagers, or information “assisting in the placing of bets or wagers on any sporting event or contest,” (2) communications that “entitle[] the recipient to receive money or credit as a result of bets or wagers,” and (3) “information assisting in the placing of bets or wagers”²⁸

One of the most striking ambiguities of the Wire Act is whether its language outlaws wagering and betting specifically on sporting events or contests across state or national boundaries, or whether it prohibits all forms of betting and wagering across state or national boundaries. This distinction is central to the question of how federal law affects the legality of Internet gambling, because the Wire Act may only reach sports betting if the limiting phrase “on any sporting event or contest,” which clearly applies to the first type of prohibited wire transmission listed in the Act, also extends to the second and third listed prohibited acts, effectively limiting the scope of the entire Wire Act to sports-specific gambling.²⁹ If it does, then online gambling via casino games such as poker, blackjack, and craps, would presumably not be prohibited by the Wire Act. For a time, there was also some question as to whether the term “wire

²⁶ *Id.*

²⁷ I. NELSON ROSE & MARTIN D. OWENS, JR., *INTERNET GAMING LAW* 74–80 (2d ed. 2009).

²⁸ 18 U.S.C. § 1084 (2012).

²⁹ The statute prohibits “bets or wagers or information assisting in the placing of bets or wagers,” but the prohibition of this behavior is specifically limited to bets on sports and contests. 18 U.S.C. § 1084(a) (2012). It is unclear whether the other two prohibitions of receiving money or credit from bets and information assisting in the placement of bets are also limited to bets on sports.

communication” applied to Internet transmissions, but it has since been settled that it does apply.³⁰

There are two cases that have explicitly considered the previous question of whether the Wire Act only applies to sports betting. *In re Mastercard International Inc.*³¹ was one case that decided on the applicability of the Wire Act. While it was ultimately affirmed by the Fifth Circuit Court of Appeals, the key analysis occurs in the district court opinion.³² In this case, credit card holders filed a class action lawsuit against several credit card companies seeking to avoid debts they incurred when they used their credit cards to purchase digital “chips” to be used at online casinos.³³ The Fifth Circuit affirmed the district court’s analysis that the “Wire Act does not prohibit non-sports [I]nternet gambling, [and] any debts incurred in connection with such gambling are not illegal.”³⁴

The District Court of Utah disagreed with the Fifth Circuit in *United States v. Lombardo*.³⁵ The defendants argued that their business, which provided out-of-state payment processing services to gambling websites, fell outside the Wire Act because the Wire Act only applied to sports betting.³⁶ The court disagreed with the defendant’s reading of the Wire Act considering the Fifth Circuit decision, but ultimately decided that the Wire Act “is not confined entirely to wire communications related to sports betting or wagering.”³⁷ The court admitted that the statute does limit the first prohibition on the interstate transmission of actual bets or wagers to those placed on sporting events or contests. However, the court

³⁰ 18 U.S.C. § 1084(a) (2012). See *United States v. Cohen*, 260 F.3d 68, 76 (2d Cir. 2001) (finding that “[*Cohen*] established two forms of wire facilities, [I]nternet and telephone,” applying the term “wire communication” to include Internet transmissions). 18 U.S.C. § 1084(a) (2012).

³¹ 313 F.3d 257 (5th Cir. 2002).

³² *In re Mastercard Int’l Inc., Internet Gambling Litig.*, 132 F. Supp. 2d 468 (E.D. La. 2001) *aff’d sub nom. In re Mastercard Int’l Inc.*, 313 F.3d 257 (5th Cir. 2002) (applying the Wire Act as written to only include sports betting and not other forms of gambling).

³³ 313 F.3d at 259–60.

³⁴ *Id.* at 263.

³⁵ 639 F. Supp. 2d. 1271 (D. Utah 2007).

³⁶ *Id.* at 1278.

³⁷ *Id.* at 1281.

declined to extend this limitation to the second and third prohibitions of interstate transactions that allow the recipient to receive money as a result of bets, or receive information assisting in placing bets.³⁸

Despite these differing court outcomes, the Department of Justice consistently interpreted the Wire Act to apply to all forms of betting and wagering until changing its interpretation in 2011.³⁹ This meant that the Department of Justice could, theoretically, prosecute Internet gambling of all kinds that crossed state lines.⁴⁰ However, use of the Wire Act in the prosecution of Internet gambling operations has typically been limited to operations of sports betting.⁴¹ In *United States v. Cohen*, the defendant, Cohen, was accused of violating the Wire Act by operating an online bookmaking business on American sports events out of Antigua.⁴² The Second Circuit affirmed Cohen's conviction for violating the Wire Act.⁴³ Cohen's business only facilitated sports betting, so the Court did not explicitly address whether the Wire Act reached other forms of online gambling.⁴⁴ The primary enforcement methods used by the Department of Justice were through publications and preemptive communications of its continuing position that the Wire Act applied to all forms of Internet gambling.⁴⁵ It should be noted, however, that few others agreed with the Department of Justice's expansive interpretation.⁴⁶ By retaining this position until 2011, the Department of Justice continued the federal government's propensity to simply prohibit gambling rather

³⁸ *Id.*

³⁹ See Rose & Bolin, *supra* note 20, at 670 (citing DOJ statements interpreting the Wire Act to apply to all gambling that involves wire transmissions); Charles P. Ciaccio, Jr., *Internet Gambling: Recent Developments and State of the Law*, 25 BERKELEY TECH. L.J. 529, 538 (2010) (citing federal prosecution under the Wire Act to show that the Department of Justice has continuously interpreted the Wire Act to apply to all gambling that involves wire transmissions). The Department of Justice's changed interpretation in 2011 is discussed in detail in Part III.D.

⁴⁰ See Rose & Bolin, *supra* note 20, at 670.

⁴¹ See *id.*; Ciaccio, *supra* note 39, at 538. The only published opinion that has found the Wire Act to cover non-sports wagering is *United States v. Lombardo*, 639 F. Supp. 2d 1271 (D. Utah 2007). See *supra* text accompanying notes 35–38.

⁴² 260 F.3d 68, 70–71 (2d Cir. 2001).

⁴³ *Id.* at 78.

⁴⁴ 260 F.3d 68.

⁴⁵ See Rose & Bolin, *supra* note 20, at 670; Romoser, *supra* note 23, at n.83.

⁴⁶ Rose & Bolin, *supra* note 20, at 670.

than attempt to control it with proper regulation. Making matters worse, the government did so by extending a “1961 law designed for telegraph wires” into the technological age of the 21st century.⁴⁷

B. *Illegal Gambling Business Act*

The Illegal Gambling Business Act of 1970⁴⁸ (the Act) provides yet another example of a law predating the Internet that currently regulates Internet gambling. The Act criminalizes the activity of “[w]hoever conducts, finances, manages, supervises, directs, or owns all or part of an illegal gambling business”⁴⁹ An “illegal gambling business” is defined as a gambling business that violates state law, involves a minimum number of people in the business, and meets a certain threshold for either length of time in operation or gross revenue.⁵⁰ This statute functions by piggybacking off of state gambling regulations.⁵¹ To violate the Illegal Gambling Business Act, one would first have to violate an underlying state law. This dependency on state law is a major difference with the Wire Act, which criminalizes its own distinct set of activities instead of relying on state law violations.⁵² In comparison with the Wire Act, one can see that the language of the Illegal Gambling Business Act is much clearer; states may set their own gambling policies, and then violations of those policies may be federally prosecuted under the Illegal Gambling Business Act. In contrast, the Wire Act confuses

⁴⁷ *Id.* at 662 (comparing it to “using stone tools to perform brain surgery—it might work, but it would be extremely messy”).

⁴⁸ 18 U.S.C. § 1955 (2012).

⁴⁹ *Id.* § 1955(a).

⁵⁰ *Id.* § 1955(b)(1)(i)–(iii). The threshold requirements are that it “(ii) involves five or more persons who conduct, finance, manage, supervise, direct, or own all or part of such business; and (iii) has been or remains in substantially continuous operation for a period in excess of thirty days or has a gross revenue of \$2,000 in any single day.” *Id.*

⁵¹ *Id.* § 1955(a). (“Whoever conducts, finances, manages, supervises, directs, or owns all or part of an *illegal* gambling business.”) (emphasis added). The Act only makes *already* illegal gambling acts illegal under federal law.

⁵² For example, the Wire Act prohibits the interstate or foreign wire transmission of sports bets, regardless of state law. *See supra* Part III.A. And, prior to the 2011 Department of Justice interpretation, it prohibited interstate Internet gambling of all forms, regardless of state law. *Id.*

state and federal power to regulate Internet gambling. Consequently, under the Wire Act, there are inconsistencies in the legality of certain Internet gambling practices.⁵³

C. *Unlawful Internet Gambling Enforcement Act of 2006*

The Unlawful Internet Gambling Enforcement Act of 2006 (UIGEA)⁵⁴ focuses on the prohibition of financial transactions related to illegal Internet gambling.⁵⁵ Somewhat controversially, the statute was “hastily tacked onto the end of unrelated legislation.”⁵⁶ Attached as Title VIII of the SAFE Port Act,⁵⁷ it states, in relevant part, that “[n]o person engaged in the business of betting or wagering may knowingly accept, in connection with the participation of another person in unlawful Internet gambling[,] . . . credit, . . . electronic fund transfer, . . . check, . . . [or] the proceeds of any other form of financial transaction”⁵⁸ It also only prohibits the transfer of money in connection with unlawful gambling, meaning that it does not reach the underlying betting activity.⁵⁹ This is congruent with the original purpose of the UIGEA, which was to target Internet gambling through its primary lifeblood—the payment systems.⁶⁰ To accomplish this, section 5364 mandates that the Secretary and Board

⁵³ States can legalize Internet gambling under their own statutes, but Internet gambling conducted between states, even if it was legal in each of the states, would violate federal law under the Wire Act. *See supra* Part III.A.

⁵⁴ 31 U.S.C. §§ 5361–67 (2012).

⁵⁵ *Id.*; *see also* Rose & Bolin, *supra* note 20, at 667.

⁵⁶ *Poker face off*, THE ECONOMIST (Apr. 20, 2011), http://www.economist.com/node/18586698?story_id=18586698&CFID=162740365&CFTOKEN=42729011; *see also* Rose & Bolin, *supra* note 20, at 667 (discussing how the UIGEA was attached to a must-pass, unrelated antiterrorist bill).

⁵⁷ The SAFE Port Act mostly regulates port security. H.R. 4954 109th Cong. (2006) (codified at 31 U.S.C. §§ 5361–67 (2012)).

⁵⁸ 31 U.S.C. § 5363(1)–(4) (2012).

⁵⁹ *See* Rose & Bolin, *supra* note 20, at 667–68 (discussing the acts that the UIGEA directly regulates, which excludes betting).

⁶⁰ 31 U.S.C. § 5361(a)(1)–(4) (2012) (Congressional finding that “Internet gambling is primarily funded through personal use of payment system instruments, credit cards, and wire transfers” and “[n]ew mechanisms for enforcing gambling laws on the Internet are necessary . . .”).

of Governors of the Federal Reserve System implement regulations that would require designated payment systems to identify and block transactions restricted under the statute.⁶¹

Given that the UIGEA prohibits participation in “unlawful Internet gambling,” the Act’s definition of that term dictates the exact activity UIGEA criminalizes:

The term “unlawful Internet gambling” means to place, receive, or otherwise knowingly transmit a bet or wager by any means which involves the use, at least in part, of the Internet where such bet or wager is unlawful under any applicable Federal or State law . . . in which the bet or wager is initiated, received, or otherwise made.⁶²

This definition illustrates a similarity with the Illegal Gambling Business Act in that the UIGEA also only criminalizes activity that is already illegal under a different law.⁶³

The UIGEA also contains exceptions that confuse and possibly undermine the Wire Act as it was interpreted by the Department of Justice until 2011. The first of such exceptions is for fantasy sports games, which could be characterized as interstate Internet gambling and therefore prohibited under the Wire Act.⁶⁴ Another exception is

⁶¹ *Id.* § 5364(a).

⁶² *Id.* § 5362(10)(A).

⁶³ The UIGEA even states that “[n]o provision of this subchapter shall be construed as altering, limiting, or extending any Federal or State law or Tribal-State compact prohibiting, permitting, or regulating gambling within the United States.” *Id.* § 5361(b).

⁶⁴ *Id.* § 5362(1)(E)(ix)(I)–(III) (stating that “[t]he term ‘bet or wager’ . . . does not include . . . participation in any fantasy or simulation sports game . . .”). For more information on fantasy sports and their relation to Internet gambling, see *The Daily Fantasy Sports Industry*, FANDUEL, <https://www.fanduel.com/legal> (last visited Aug. 15, 2014) (identifying that most states consider fantasy sports a game of skill and therefore legal, but not offering paid entry of daily fantasy sports games to residents of Arizona, Iowa, Louisiana, Montana, and Washington, where the legality of fantasy sports is unclear or questionable); see also Matt Hunt, *How Fantasy Football Works*, HOW STUFF WORKS, <http://entertainment.howstuffworks.com/fantasy-football.htm> (last visited Aug. 15, 2014) (providing an overview of fantasy football, including the rise of its

found within the statute's definition of unlawful Internet gambling, where it excludes intrastate Internet gambling as long as it is in accordance with the laws of the state in which the gambling occurs and the bet is initiated and received within that state's borders.⁶⁵ In addition, the UIGEA specifies that "[t]he intermediate routing of electronic data shall not determine the location or locations in which a bet or wager is initiated, received, or otherwise made."⁶⁶ Thus, an apparent conflict exists between the permissible interstate routing of electronic data related to otherwise lawful, intrastate Internet gambling under the UIGEA and the Wire Act's prohibition of *all* interstate transmissions related to acts of gambling.⁶⁷ This uncertainty surrounding the state of federal law became the landscape in which Internet gambling operators either safely withdrew from or risked remaining in the United States market.

The effect of the UIGEA was swift and ruthless; with its passage, many public companies shut down websites for gambling in the United States.⁶⁸ The world's largest online poker provider, PartyGaming, stated on October 2, 2006 that it would leave the United States market when the UIGEA took effect.⁶⁹ On December 16, 2008, one of the founders of PartyGaming, Anurag Dikshit, pled guilty to using "wires to transmit bets and wagering information."⁷⁰

popularity as an Internet game in which participants pay money to play and receive winnings if they prevail).

⁶⁵ 31 U.S.C. § 5362(10)(B)(i)–(ii) (2012).

⁶⁶ *Id.* § 5362(10)(E).

⁶⁷ See Rose & Bolin, *supra* note 20, at 671–72 (discussing the conflict between the Wire Act and the UIGEA). Compare *supra* p. 539 and notes 65–66 (providing a UIGEA exception to illegal Internet gambling for legal, intrastate Internet gambling that is conducted within state borders, regardless of whether electronic data related to the gambling is intermediately routed out-of-state), with 18 U.S.C. § 1084 (2012) (prohibiting interstate wire transmissions related to gambling).

⁶⁸ Heather Timmons & Eric Pfanner, *U.S. Law Causing Turmoil in Online Gambling Industry*, N.Y. TIMES, Nov. 1, 2006, <http://www.nytimes.com/2006/11/01/business/01gamble.html>.

⁶⁹ Kate Norton, *Party's Over for Online Gambling*, BLOOMBERG BUSINESSWEEK, (Oct. 2, 2006), <http://www.businessweek.com/stories/2006-10-02/party-s-over-for-online-gamblingbusinessweek-business-news-stock-market-and-financial-advice>.

⁷⁰ Press Release, U.S. Att'y S. Dist. of N.Y., Partygaming Founder Pleads Guilty in Internet Gambling Case and Agrees to \$300 Million Forfeiture (Dec. 16, 2008), *available at*

Part of Dikshit's plea agreement was a fine for \$300 million.⁷¹ Though this prosecution occurred after the enactment of the UIGEA, the plea agreement did not mention the UIGEA, and the language indicates that the charges were for violations of the Wire Act.⁷² Then in April of 2009, PartyGaming signed a non-prosecution agreement with the Department of Justice in exchange for an admission that it provided Internet gambling services to United States customers prior to the enactment of the UIGEA, and payment of a \$105 million fine.⁷³ Also, in 2009, in an unprecedented move, the Department of Justice seized bank accounts of 27,000 online poker players worth at least \$33 million.⁷⁴ This federal enforcement, like the previous PartyGaming prosecutions, appeared to cite violations of the Wire Act and Illegal Gambling Business Act rather than the UIGEA.⁷⁵ Although these enforcement efforts did not arise out of clear UIGEA violations, it seems that the passage of the UIGEA may have encouraged them.

In 2011, the largest federal crackdown against Internet gambling, dubbed "Black Friday" by online poker connoisseurs, shut down three of the largest online poker websites still operating in the United States.⁷⁶ On April 15, 2011, the United States Attorney for the Southern District of New York issued an indictment against PokerStars, Full Tilt Poker, and Absolute Poker (collectively, the Poker Companies), charging them with bank fraud, illegal gambling

<http://www.justice.gov/usao/nys/pressreleases/December08/dikshitanuragpleapr.pdf>.

⁷¹ *Id.*

⁷² *Id.*; see also *History of Party Poker Part of Partygaming*, GAMBLING SITES, <http://www.gamblingsites.com/history/partygaming/> (last visited Sept. 15, 2014) (stating that Dikshit was guilty for violating the Wire Act prior to the introduction of the UIGEA).

⁷³ Jennifer Newell, *PartyGaming Settles with U.S. Dept. of Justice for \$105 Million*, BLUFF HOLDING COMPANY (Apr. 7, 2009), <http://www.bluff.com/news/partygaming-settles-with-us-dept-of-justice-for-105-million-3012/>.

⁷⁴ Matt Richtel, *Web's Poker Winners Face Delays in Collecting*, N.Y. TIMES, June 9, 2009, http://www.nytimes.com/2009/06/10/business/10poker.html?_r=2&.

⁷⁵ Russell Goldman, *Feds Freeze Poker Champ's Winnings*, ABC NEWS, June 11, 2009, <http://abcnews.go.com/Business/story?id=7808131&page=2>.

⁷⁶ Matt Richtel, *U.S. Cracks Down on Online Gambling*, N.Y. TIMES, Apr. 15, 2011, http://www.nytimes.com/2011/04/16/technology/16poker.html?_r=0.

offenses, and laundering billions of dollars in illegal gambling proceeds.⁷⁷ Because United States' banks and credit card issuers would not process the Poker Companies' payments for Internet poker, the companies developed payment processors that would circumvent the UIGEA and deceive these financial institutions.⁷⁸ The defendants, the Poker Companies, allegedly used individual payment processors for online poker credits that were disguised as payments to nonexistent online merchants for legal goods.⁷⁹ The Department of Justice seized the website domains of the Poker Companies and terminated their Internet poker operations in the United States.⁸⁰ On July 31, 2012, the case against the Poker Companies settled.⁸¹ Pursuant to the settlement agreement, PokerStars acquired FullTilt in a merger and paid the sum of \$547 million to the federal government.⁸² Five years after Congress enacted the UIGEA, these events culminated in what would be remembered as one of the largest government shutdowns of Internet gambling arising out of UIGEA violations.⁸³

D. Department of Justice Office of Legal Counsel Memorandum

On December 23, 2011, the Office of Legal Counsel (OLC), under the Department of Justice, released a memo (OLC Memo) in

⁷⁷ Press Release, U.S. Att'y S. Dist. of N.Y., Manhattan U.S. Att'y Charges Principals of Three Largest Internet Poker Cos. with Bank Fraud, Illegal Gambling Offenses and Laundering Billions in Illegal Gambling Proceeds (Apr. 15, 2011), *available at* <http://www.justice.gov/usao/nys/pressreleases/April11/scheinbergetalindictmentpr.pdf>.

⁷⁸ *Id.*

⁷⁹ *Id.*

⁸⁰ *Id.*

⁸¹ Gary Wise, *PokerStars settles, acquires FTP*, ESPN POKER, http://espn.go.com/poker/story/_/id/8218085/pokerstars-reaches-settlement-department-justice-acquires-full-tilt-poker (last updated July 31, 2012, 5:25 PM).

⁸² *Id.* In the settlement, PokerStars did not admit to any wrongdoing and retained the right to apply for an Internet gambling license in the future when regulations are enacted. *Id.*

⁸³ Andrew Feldman, *Sites charged with gambling offenses*, ESPN POKER, <http://sports.espn.go.com/espn/poker/news/story?id=6362238> (last updated Apr. 16, 2011, 11:33 AM).

response to inquiries by the states of Illinois and New York regarding the lawfulness of selling lottery tickets over the Internet to in-state adults using out-of-state transaction processors.⁸⁴ The OLC Memo reversed the Department of Justice's interpretation of the Wire Act by concluding: "interstate transmissions of wire communications that do not relate to a 'sporting event or contest' . . . fall outside of the reach of the Wire Act. Because the proposed New York and Illinois lottery proposals do not involve wagering on sporting events or contests, the Wire Act does not . . . prohibit them."⁸⁵

The OLC Memo also briefly discussed, but failed to definitively resolve, the specific question raised by New York and Illinois regarding the interplay between the Wire Act and the UIGEA. This question was whether the Wire Act "may prohibit States from conducting in-state lottery transactions via the Internet if the transmissions over the Internet during the transaction cross State lines, and may also limit States' abilities to transmit lottery data to out-of-state transaction processors."⁸⁶ In their inquiries, New York and Illinois expounded upon the issue by addressing the conflict between the Wire Act and the UIGEA:

[The] UIGEA appears to permit intermediate out-of-state routing of electronic data associated with lawful lottery transactions that otherwise occur in-state. In light of this apparent conflict, [New York and Illinois] have asked whether the Wire Act and UIGEA prohibit a state-run lottery from using the Internet to sell tickets to in-state adults where the transmission using the Internet crosses state lines, and whether these statutes prohibit a state lottery from transmitting lottery data associated with in-state ticket sales to an

⁸⁴ *Whether Proposals by Illinois and New York to Use the Internet and out-of-State Transaction Processors to Sell Lottery Tickets to in-State Adults Violate the Wire Act*, 35 Op. O.L.C. 1-2 (Sept. 20, 2011), available at <http://www.justice.gov/sites/default/files/olc/opinions/2011/09/31/state-lotteries-opinion.pdf> [hereinafter OLC Memo].

⁸⁵ *Id.* at 1-2.

⁸⁶ *Id.*

out-of-state transaction processor either during or after the purchasing process.⁸⁷

The OLC Memo responded by only confirming that the Wire Act does not reach communications that do not relate to a sporting event or contest.⁸⁸ Even while coming to a conclusion in favor of New York and Illinois, and allowing the two states to conduct their online lotteries without fear of federal prosecution, the Office of Legal Counsel failed to address the concern of a possible conflict between the Wire Act and UIGEA stating, “[W]e have not found it necessary to address the Wire Act’s interaction with UIGEA, or to analyze UIGEA in any other respect.”⁸⁹ The resolution of this specific issue was seemingly unnecessary, given that the OLC Memo declared that the Wire Act did not apply to the otherwise legal activity in question.⁹⁰ Regardless, the changed interpretation of the Wire Act eliminated a significant federal barrier to state legalization of Internet gambling for games such as poker, blackjack, and craps. With this new interpretation, Internet gambling providers, financial institutions, transactions processors, and states no longer needed to worry about federal prosecution of Internet gambling and related transactions that crossed state lines, as long as the Internet gambling was legal in each jurisdiction in which the bets were initially placed and ultimately received.⁹¹

E. Current State of the Law

To recap: prior to 2011, the Wire Act prohibited wire transmissions in interstate or foreign commerce relating to (1) bets, wagers, or information assisting in the placing of bets or wagers on any sporting event or contest, (2) communications that entitle the recipient to receive money or credit as a result of bets or wagers, and

⁸⁷ *Id.*

⁸⁸ *Id.*

⁸⁹ *Id.* at 2.

⁹⁰ *Id.* at 13 (“[W]e need not consider how to reconcile the Wire Act with UIGEA, because the Wire Act does not apply in this situation. Accordingly, we express no view about the proper interpretation or scope of UIGEA.”).

⁹¹ *Supra* p. 542 and notes 84–85; *accord supra* p. 539 and notes 65–67.

(3) information assisting the placing of bets or wagers.⁹² The Department of Justice maintained that the Wire Act applied to both sports bets and all other forms of Internet gambling.⁹³ Though the Department of Justice maintained this interpretation, federal courts were split as to whether the Wire Act should apply only to sports gambling or to all forms of gambling.⁹⁴ The enactment of the UIGEA in 2006 added to the Wire Act's prohibition of interstate or foreign transmissions involving Internet gambling by prohibiting financial transactions in connection with unlawful Internet gambling.⁹⁵ However, the UIGEA contains a critical provision, which states that "[t]he intermediate routing of electronic data shall not determine the location or locations in which a bet or wager is initiated, received, or otherwise made."⁹⁶ This means that the UIGEA differentiates between placing, receiving, or transmitting bets and the intermediate routing of data occurring in bank transfers or financial processing transactions. Thus, in contrast to the Wire Act, under the UIGEA, only the placing, receiving, or transmitting of bets is relevant for determining the location of where the gambling takes place.

Before reading New York's and Illinois's concerns in the OLC Memo, one might consider whether states could comply with the Wire Act, even if it were applied to all forms of Internet gambling (as it was interpreted before 2011) by keeping the entire process of Internet gambling within state lines. While it is possible to enforce the placing of bets within states lines, as a practical matter, it is much more difficult, if not impossible, to ensure that every payment, processor transaction, bank transfer, or other wire communication relating to the operation of Internet gambling remains exclusively within a single state's jurisdiction.⁹⁷ Until 2011, this was a

⁹² See *supra* Section III.A.

⁹³ See *supra* p. 535 and note 39.

⁹⁴ See *supra* pp. 534–535 notes 32–38 (the Fifth Circuit in *In Re Mastercard Int'l Inc.* found that the Wire Act did not apply to non-sports Internet gambling, whereas the District of Utah disagreed, stating that the Wire Act did not apply only to sports gambling).

⁹⁵ See *supra* Section III.C.

⁹⁶ 31 U.S.C. § 536210)(E) (2012).

⁹⁷ OLC Memo, *supra* note 84, at 2. This was the concern of New York and Illinois in their appeal to the Office of Legal Counsel:

significant barrier to state legalization of Internet gambling.⁹⁸ Then, in 2011, the OLC Memo reinterpreted the Wire Act to apply to only wagering on sports events or contests.⁹⁹ This meant that the transmissions of financial or gambling information that made Internet gambling so difficult to keep within state lines no longer needed to be confined within a single state's jurisdiction. Thus, federal law now provides that as long as the placing of bets occurs exclusively in jurisdictions where online gambling is legal, the activity is legal.¹⁰⁰ Since 2011, the Wire Act's clout with regard to prohibiting intrastate Internet gambling is significantly diminished, leaving the UIGEA and the Illegal Gambling Business Act as the primary federal enforcement statutes against illegal Internet gambling—and these statutes only bootstrap off of existing state law.¹⁰¹ Thus, if a state legalizes Internet gambling, the activity is legal and in accordance with federal law, as long as the gambling itself occurs within state lines or other jurisdictions where the activity is legal. The electronic transmissions connected with Internet gambling, such as bank transfers and payment processors, no longer need to be confined within state lines, given that the Wire Act no longer makes them illegal and they are not implicated in the UIGEA or the Illegal Gambling Business Act.¹⁰² As stated above, the OLC memo did not explicitly make this finding (it declined to analyze the UIGEA any further).¹⁰³ However, New York and Illinois were permitted to run their Internet lotteries in state while transmitting data associated with

New York is finalizing construction of a new computerized system that will control the sale of lottery tickets to in-state customers. . . . New York also notes that all transaction data in the new system will be routed from the customer's location in New York to the lottery's data centers in New York and Texas through networks controlled in Maryland and Nevada. . . . Illinois characterizes its program as "an intrastate lottery, despite the fact that packets of data may intermediately be routed across state lines over the Internet."

Id. (citations omitted).

⁹⁸ See *supra* p. 542 and notes 84–85; *accord supra* p. 539 and notes 65–67.

⁹⁹ See *supra* p. 542 and notes 84–85.

¹⁰⁰ See *supra* p. 542 and notes 84–85; *accord supra* p. 539 and notes 65–67.

¹⁰¹ See *supra* Section III.D.

¹⁰² See *supra* Section III.B–D.

¹⁰³ See *supra* p. 543 and notes 88–89.

the online ticket sales to out-of-state transaction processors. Therefore, the effect of the memo replaced the need for any such explicit finding, and the resulting inference described above has not been refuted by the Department of Justice in any way.¹⁰⁴

As illustrated by this section, federal laws have often been unclear, and their enforcement has been unpredictable and inconsistent. Regulation cannot operate effectively in this way if the goal is to maximize the benefits that the Internet gambling industry can offer the United States. The following section will outline states' regulatory schemes regarding Internet gambling and the recent trend of legalization in several states. One will see that an industry as large and complex as Internet gambling demands an overarching federal regulatory system, especially in light of developing state regulation and the resulting regulatory inconsistencies.

IV. STATE REGULATION OF INTERNET GAMBLING

States have historically served as "laboratories" for the federal government in testing novel economic, social, and regulatory "experiments."¹⁰⁵ The OLC Memo opened the door for states to legalize Internet gambling, giving them freedom to explore the frontier of Internet gambling regulation. Thus far, the states of Nevada, Delaware, and New Jersey have legalized and regulated Internet gambling.¹⁰⁶ In addition, the states of Illinois and Georgia have introduced the sale of lottery tickets over the Internet.¹⁰⁷ These

¹⁰⁴ See *supra* pp. 542–543 and notes 85–88.

¹⁰⁵ This phrasing was first popularized in a dissenting opinion authored by Justice Louis Brandeis. See *New State Ice Co. v. Liebmann*, 285 U.S. 262, 311 (1932) (Brandeis, J., dissenting) ("To stay experimentation in things social and economic is a grave responsibility. Denial of the right to experiment may be fraught with serious consequences to the nation. It is one of the happy incidents of the federal system that a single courageous state may, if its citizens choose, serve as a laboratory; and try novel social and economic experiments without risk to the rest of the country. This Court has the power to prevent an experiment.").

¹⁰⁶ 2013 *Legislation Regarding Internet Gambling or Lotteries*, NATIONAL CONFERENCE OF STATE LEGISLATURES, <http://www.ncsl.org/research/financial-services-and-commerce/2013onlinegamblinglegislation.aspx> (last updated Dec. 20, 2013).

¹⁰⁷ *Id.*

state “experiments” have important implications for future federal legislation and regulation of Internet gambling.

A. *Nevada*

Housing the gambler’s paradise of Las Vegas within its jurisdiction, the state of Nevada has long been a champion for the legalization and regulation of the gambling industry, including Internet gambling. Nevada was the first state to legalize online gambling when Governor Brian Sandoval signed Assembly Bill No. 114 into law on February 21, 2013.¹⁰⁸ The regulatory system established by this statute has many practical and beneficial features that a federal regulatory scheme could adopt.

The Nevada statute operates by adding the regulation of interactive gaming to the Nevada Gaming Commission’s jurisdiction.¹⁰⁹ Under the Commission’s oversight, the statute establishes fees for licenses to operate interactive gaming and to manufacture systems and equipment associated with interactive gaming.¹¹⁰ In Nevada, initial licenses to operate interactive gaming last for two years and cost \$500,000, and license renewal fees for the immediately following one-year period cost \$250,000.¹¹¹ In addition

¹⁰⁸ A.B. 114, 77th Assemb., Reg. Sess. (Nev. 2013); *see also Nevada Legalizes Online Gambling*, CBS NEWS, (Feb. 22, 2013), <http://www.cbsnews.com/news/nevada-legalizes-online-gambling/>.

¹⁰⁹ NEV. REV. STAT. § 463.750(1) (2013). The Nevada statute uses the language “interactive gaming” instead of “Internet gambling,” but the terms have the same meaning for the purposes of this article. There are different terms used for Internet gambling throughout state and federal statutes and academia, but they all essentially mean gambling of any form conducted on the Internet.

¹¹⁰ *Id.* §§ 463.760–65.

¹¹¹ *Id.* § 463.765(1)(a)–(d). The Nevada Gaming Commission is also authorized by statute to raise the initial license fee to up to \$1,000,000 and renewal license fee to \$500,000 for various reasons, including: ensuring licensees have the financial capacity to operate interactive gaming, compensation for regulatory costs that require additional personnel or other regulatory expenditures, compensation for increased costs due to entering an interactive gaming agreement with other states, or compensation for federal legislation that necessitate or make advisable a higher licensing fee. *Id.* § 463.765(2)(a)–(d). The initial one-year license fee for a manufacturer of interactive gaming systems is \$125,000. *Id.* § 463.760(1)(a), (2). For a manufacturer of equipment associated with interactive gaming, the initial

to the obvious revenue they generate, these hefty licensing fees ensure that licensees have the financial capacity to successfully operate an Internet gambling enterprise; this is a cautionary feature that a federal regulatory system should incorporate.¹¹²

A unique aspect of Nevada's regulation of Internet gambling is that, in several instances, it extends pre-established regulations governing its "brick-and-mortar" casinos to regulate Internet gambling.¹¹³ For example, Nevada taxes Internet gambling revenue at the same monthly rate as brick-and-mortar casino revenue.¹¹⁴ Nevada taxes gross revenue generated by gambling monthly at the maximum rate of 6.75%.¹¹⁵ These licensing fees and taxes on revenue are substantial considerations for states deciding whether to legalize and regulate Internet gambling.¹¹⁶

Another example in which Nevada builds its Internet gambling regulation from its preexisting gambling laws is the requirement that a license applicant must already be in the casino business and not have operated any interactive gaming activity in violation of state or

one-year license fee is \$50,000. *Id.* § 463.760(1)(b), (2). For both manufacturers, one-year renewal license fees are each \$25,000. *Id.* § 463.760(2)–(3).

¹¹² See generally John Wilkerson, *Nevada Approves Internet Gambling*, ABC NEWS (June 4, 2001), <http://abcnews.go.com/US/story?id=93177> (Senate Judiciary Chairman Mark James R-Las Vegas, a proponent of early Internet gambling legislation, "said the \$500,000 fee ensures that reputable companies undertake Internet gambling." Of course, opponents, such as Senator Terry Car, D-Las Vegas, have the differing opinion that the high licensing "fee[s] for Internet gambling makes it impossible for small casinos and entrepreneurs to participate.").

¹¹³ "Brick-and-mortar" is a term used for casinos in physical buildings.

¹¹⁴ NEV. REV. STAT. § 463.370 (2013).

¹¹⁵ *Id.* § 463.370(1)(c). There is a tiered structure governing the rate at which gross revenue is taxed: 3.5% for gross revenue not exceeding \$50,000 per calendar month, 4.5% for gross revenue exceeding \$50,000, but not \$134,000, per calendar month, and 6.75% of gross revenue exceeding \$134,000 per calendar month. *Id.* § 463.370(1)(a)–(c).

¹¹⁶ See, e.g., *Authorizing Online Poker in California*, LEGISLATIVE ANALYST'S OFFICE 1, 7, 9–11 (Apr. 23, 2014), <http://www.lao.ca.gov/handouts/education/2014/Authorizing-Online-Poker-in-California-042314.pdf> (analyzing the potential gross revenue that legalized online poker in California could generate and the various factors affecting such revenue).

federal law to obtain an interactive gaming license.¹¹⁷ Due to these limits, only entities that have previous experience in legal gaming operations will be able to operate interactive gaming.

One of the Commission's most important responsibilities in the administration and regulation of Nevada's interactive gaming is setting forth the "standards for the location and security of the computer system and for approval of hardware and software used in connection with interactive gaming."¹¹⁸ This technical compliance aspect of regulation, paired with strict licensing investigation standards, is instrumental to "ensure the protection of consumers, including minors and vulnerable persons, prevent fraud, guard against underage and problem gambling, avoid unauthorized use by persons located in jurisdictions that do not authorize interactive gaming[,] and aid in law enforcement efforts."¹¹⁹ These regulatory safeguards and the use of a central Internet gambling regulatory commission to enforce the regulations should be incorporated in a prospective federal regulatory system.

Though there are many different licensed service providers and gaming manufacturers that comprise Nevada's Internet gambling infrastructure, only three Interactive Gaming Operator licenses have been issued by the Gaming Control Board.¹²⁰ These licenses have been issued to Caesars Interactive Entertainment, Inc., Fertitta Interactive LLC, and South Point Poker LLC.¹²¹ Despite the issuance

¹¹⁷ NEV. REV. STAT. § 463.750(3)–(9) (2013). The statute does, however, provide flexibility to the Commission to waive these requirements at its discretion. *Id.*

¹¹⁸ *Id.* § 463.750(2)(f).

¹¹⁹ *Id.* § 463.745(2) (promulgating the fundamental goals of the regulatory structure).

¹²⁰ See *Interactive Gaming/Service Providers*, NEV. STATE GAMING CONTROL BD. GAMING COMM'N, <http://gaming.nv.gov/index.aspx?page=259> (last visited Aug. 15, 2014). For a complete list of licensed interactive gaming manufacturers, see *Mfg Inter. Gaming Systems, Active*, STATE OF NEV. GAMING CONTROL BD., <http://gaming.nv.gov/modules/showdocument.aspx?documentid=7280> (last updated Sept. 5, 2014, 1:09 PM). For a complete list of licensed interactive gaming service providers, see *Listing of Locations*, STATE OF NEV. GAMING CONTROL BD., <http://gaming.nv.gov/modules/showdocument.aspx?documentid=7279> (last updated Sept. 5, 2014, 1:10 PM).

¹²¹ *Interactive Gaming/Service Providers*, *supra* note 120. For an updated list, see *Operator Inter. Gaming, Active*, STATE OF NEV. GAMING CONTROL BD.,

of these licenses, Nevada “has just two poker-only Internet gaming sites.”¹²² In contrast to New Jersey, Nevada (the first state to legalize Internet gambling) has been deliberate in expanding its Internet gambling industry to include casino games other than poker and additional licensed operators.¹²³

B. *New Jersey*

New Jersey enacted legislation regulating Internet gambling on February 26, 2013, just after Nevada.¹²⁴ These statutes are unique in that they specifically confine all operations of Internet gambling to Atlantic City, the only jurisdiction in New Jersey where casinos are lawfully permitted to operate.¹²⁵ Few aspects of New Jersey’s regulation differ from Nevada’s, and the basic goals of each are the same.

New Jersey’s regulatory bodies consist of the New Jersey Casino Control Commission¹²⁶ and the Division of Gaming Enforcement.¹²⁷ The two share regulatory, licensing, enforcement, and adjudicatory authority over Internet gambling activities in the state.¹²⁸ This division of labor is similar to Nevada’s two-tiered regulatory structure.¹²⁹ Also, as in Nevada, entities wishing to operate an

<http://gaming.nv.gov/modules/showdocument.aspx?documentid=7912> (last updated Sept. 5, 2014, 1:11 PM).

¹²² Howard Stutz, *Wynn gets OK for online gambling in New Jersey, puts efforts on hold*, LAS VEGAS REVIEW-JOURNAL (Feb. 3, 2014), <http://www.reviewjournal.com/business/wynn-gets-ok-online-gambling-new-jersey-puts-efforts-hold>.

¹²³ See *infra* Section IV.B.

¹²⁴ N.J. STAT. ANN. §§ 5:12–95.17–33 (2013).

¹²⁵ *Id.* § 5:12–95.17 k; see also N.J. CONST. art. IV, § 7, ¶ 2 D.

¹²⁶ Created by N.J. STAT. ANN. § 5:12–50 (2012).

¹²⁷ Created by *id.* § 5:12–55.

¹²⁸ The Casino Control Commission has the authority to decide on license applications, review complaints by licensees, and decide appeals from violation and penalty assessment. *Id.* § 5:12–63. The Division of Gaming Enforcement leads investigations of license applicants, oversees hearings concerning gaming conduct operations, and enforces all gaming laws. *Id.* § 5:12–76.

¹²⁹ Nevada’s two regulatory bodies are the Gaming Commission and the State Gaming Control Board. See NEV. REV. STAT. § 463.140 (2013). Similar to the way the regulatory bodies operate in New Jersey, in Nevada, one generally controls licensing and the other is generally the prosecutorial authority. *Id.* The Gaming

Internet gambling business in New Jersey must already have a valid brick-and-mortar casino license.¹³⁰ An initial, one-year licensing fee costs at least \$400,000, and annual renewal fees are no less than \$250,000.¹³¹ New Jersey's taxation of Internet gambling is based on gross revenue, which is subject to an annual 15% tax.¹³² In contrast, New Jersey casinos are taxed at just 8% of gross revenues.¹³³ This disparate tax treatment of Internet gambling is a notable departure from Nevada's taxation approach.¹³⁴

New Jersey's basic regulatory goals in its legislative findings and declarations are fairly similar to Nevada's in that they highlight the importance of inhibiting wagering by underage or otherwise vulnerable individuals and ensuring that Internet games are fair and safe through the use of approved hardware and software.¹³⁵ Additionally, New Jersey emphasizes the policy reason of ending "the practice of sending much-needed jobs and tax revenue overseas to illegal operators while creating jobs and economic development in Atlantic City" for legalizing and regulating Internet gambling.¹³⁶ This is a strong incentive for many states in efforts to legalize and regulate online gambling; the most effective way to take advantage of an industry is to eliminate its unlicensed operators.

New Jersey has quickly licensed a multitude of Internet gambling operators since November 21, 2013, when Internet gambling went live in the state.¹³⁷ As of February 3, 2014, a total of sixteen

Commission controls licensing and acts in a judicial capacity to discipline entities for violations. *Id.* The Gaming Control Board is the prosecutorial authority in disciplinary procedures against a gaming license. *Id.*

¹³⁰ N.J. STAT. ANN. § 5:12-95.21 (2013).

¹³¹ *Id.* § 5:12-95.29(a).

¹³² *Id.* § 5:12-95.19.

¹³³ *Id.*

¹³⁴ Compare *id.* § 5:12-95.29(a) (setting forth a 15% annual tax rate for Internet gambling, which is nearly double the tax rate for brick-and-mortar casino gambling), with NEV. REV. STAT. § 463.370 (2013) (taxing Internet gambling and brick-and-mortar casino gambling at the same monthly rate of 6.75%).

¹³⁵ N.J. STAT. ANN. § 5:12-95.17(h) (2013).

¹³⁶ *Id.*

¹³⁷ *New Jersey Becoming 3rd State To Offer Internet Gambling*, CBS NEW YORK (Nov. 21, 2013, 12:45 PM), <http://newyork.cbslocal.com/2013/11/21/new-jersey-becoming-3rd-state-to-offer-internet-gambling/> ("A five-day trial period of

“transactional waivers” have been issued to companies authorizing engagement in Internet gambling activities.¹³⁸ Among these companies are Caesars and Amaya, Tropicana and Gamesys, Bally’s and 888, Trump Taj Mahal and Ultimate Gaming/CAMS, Golden Nugget and Bally Technologies/Amaya, Borgata and bwin.party/Amaya/CAMS, and Trump Plaza and Betfair/GameAccount/Amaya/CAMS.¹³⁹ The two largest-grossing companies thus far have been the Borgata Hotel Casino & Spa and Caesars Interactive, which accounted for about three quarters of New Jersey’s Internet gambling tax revenue in 2013.¹⁴⁰

C. Online Lotteries

Several states have not fully committed to legalizing all forms of Internet gambling in their jurisdictions, but have upgraded their lottery systems to enable online purchases. Currently, only Illinois

Internet gambling begins at 6 p.m. Thursday when players invited by casinos to test their systems make real-money bets online.”).

¹³⁸ See *INTERNET GAMING Companies Issued a Transactional Waiver*, NEW JERSEY DIVISION OF GAMING ENFORCEMENT, <http://www.nj.gov/oag/ge/docs/InternetGaming/TransactionWaivers/RelatedTransactionWaivers.pdf> (last updated Feb. 3, 2014). As of December 11, 2013, there are only eight Internet gaming permit holders (the number is smaller because, as explained above, Internet gambling operators must already have a valid brick-and-mortar casino license): Borgata Hotel Casino & Spa, Golden Nugget Atlantic City, Trump Plaza Associates, Trump Taj Mahal Associates, Tropicana Casino and Resort, Caesars Interactive Entertainment New Jersey as the affiliate of Bally’s Park Place, Caesars Interactive Entertainment New Jersey as the affiliate of Boardwalk Regency Corporation, and DGMB Resorts Casino Hotel. See *INTERNET GAMING PERMIT HOLDERS*, NJ.GOV, <http://www.nj.gov/oag/ge/docs/InternetGaming/internetgamingpermitholders.pdf> (last updated Aug. 25, 2014).

¹³⁹ Chris Grove, *New Jersey Expands Online Gambling Approval List*, ONLINE POKER REPORT (Nov. 15, 2013), <http://www.onlinepokerreport.com/9109/new-jersey-expands-online-gambling-approval-list/>.

¹⁴⁰ *NJ Online Gambling Revenues Come In Below Expectations*, CBS NEW YORK (Jan. 15, 2014, 11:54 AM), <http://newyork.cbslocal.com/2014/01/15/nj-online-gambling-revenues-come-in-below-expectations/> (“The figures also show New Jersey’s fledgling Internet gambling industry being dominated by two main players: the Borgata Hotel Casino & Spa and Caesars Interactive, which together won \$6.1 million of the \$8.4 million that was taken in by New Jersey Internet gambling sites over the year’s final five weeks.”).

and Georgia have Internet lotteries with the potential for expansion into other online gaming.¹⁴¹ In contrast, Delaware has legalized Internet gambling for numerous table games—such as poker—in addition to online lottery sales through its state-run lottery program.¹⁴² These three distinct jurisdictions are good examples of how states are in various stages of legalization, demonstrating the utility of an overarching federal regulatory scheme in providing consistency nationwide.

Georgia is the least likely of these three states to legalize other forms of Internet gambling, aside from an online lottery, because it has the least favorable political climate for such expansion.¹⁴³ Influential interest groups and Georgia's political leadership are generally against the expansion of gambling in the state; even the incremental expansion to an online ticketing system for the state's lottery has been met with opposition.¹⁴⁴ As expected, the sale of lottery tickets online is accompanied by strict regulation. These regulations include mandatory player registration and monitoring of IP addresses to verify that players making purchases are physically located in Georgia, banking requirements, and playing time limits.¹⁴⁵ Interestingly, unlike states that permit some form of Internet gambling, Georgia's regulations are not established by statute; the

¹⁴¹ 2013 Legislation Regarding Internet Gambling and Lotteries, NATIONAL CONFERENCE OF STATE LEGISLATURES, <http://www.ncsl.org/research/financial-services-and-commerce/2013onlinegamblinglegislation.aspx> (last updated Dec. 20, 2013); see also 20 ILL. COMP. STAT. 1605/7.12 (2013) (establishing Illinois's Internet lottery pilot program); Jean Ross, *Georgia Online Lottery Approved*, CBS ATLANTA (June 23, 2012), <http://atlanta.cbslocal.com/2012/07/23/georgia-online-lottery-approved/>.

¹⁴² DEL. CODE ANN. tit. 29, § 4803(k) (2013) (defining Internet lottery as encompassing Internet ticket games, the Internet video lottery and Internet table games); *id.* § 4826(a) (authorizing the Director of the State Lottery Office to operate an Internet lottery).

¹⁴³ Ross, *supra* note 141.

¹⁴⁴ *Id.* “The Georgia Family Council has expressed disappointment that the ticket sales will be expanded, describing the lottery system as ‘inherently exploitative.’ . . . Governor Nathan Deal, though opposed to the expansion of gambling in Georgia, said Thursday that he is okay with online ticket sales.” *Id.* (internal quotation marks omitted).

¹⁴⁵ *Id.*

approval of the online ticketing system and implementation of regulatory controls came from state lottery officials.¹⁴⁶

Illinois, on the other hand, enacted a specific statute, entitled the “Internet pilot program,” effective August 16, 2013, which authorized the online sale of lottery tickets.¹⁴⁷ Similar to Georgia, it contemplated regulatory requirements such as ensuring that sales are made solely within the state of Illinois by persons eighteen years of age or older and limiting the amount of purchases by any one person’s lottery account.¹⁴⁸ The pilot program, as suggested by its title, is only temporary—lasting between three and four years—after which time the Lottery Study Committee will evaluate and analyze the various effects of online lottery sales.¹⁴⁹

The state of Delaware, meanwhile, ranks along with Nevada and New Jersey as one of the leaders in state legalization of Internet gambling, in part because Delaware has legalized all forms of Internet gambling through its Internet lottery statute.¹⁵⁰ As with other states with legalized online gambling, the Delaware statute provides for regulatory safeguards.¹⁵¹ Delaware’s approach to legalization is unique from other states’ approaches in that licensing fees for service providers and operators are nominal, and the gaming is strictly regulated and controlled by the Delaware State Lottery Office.¹⁵² Instead of collecting larger licensing fees for the operation

¹⁴⁶ *Id.*

¹⁴⁷ 20 ILL. COMP. STAT. 1605/7.12 (2013).

¹⁴⁸ *Id.* § 7.12(b).

¹⁴⁹ *Id.* § 7.12(b)–(c). Some of the effects to be evaluated and analyzed include: economic benefits to the state, local governments, and lottery retailers; player age verification; control of gambling addiction; technological, programming, and security requirements; and cost and project time estimates for implementation. *Id.* § 7.12(c)(1)–(9).

¹⁵⁰ See DEL. CODE ANN. tit. 29, § 4803(k) (2013) (Internet lottery defined to encompass Internet ticket games, the Internet video lottery and Internet table games); *id.* § 4826(a) (authorizing the Director of the State Lottery Office to operate an Internet lottery).

¹⁵¹ DEL. CODE ANN. tit. 29, § 4826(c)(1)–(8) (2012). Specifically, these safeguards include: verification of age and location of players, procedures of financial transactions and transfers, and procedures for security and reliability of online games. *Id.*

¹⁵² See DEL. CODE ANN. tit. 29, § 4803(r), (k) (2013) (section 4803(r) defines “Office” as the State Lottery Office, and section 4803(k) defines “Internet Lottery”

of Internet gambling and taxes on gross revenue, under the Delaware Gaming Competitiveness Act of 2012, Delaware collects all gross revenue from Internet gambling (less winnings paid to players) and deposits it in the “State Internet Lottery Fund,” which is then distributed pursuant to title 29, section 4815 of the Delaware Code.¹⁵³ From this distribution, Delaware receives about 44% of Internet slots revenue and 29% of revenue from all other games, excluding payments made to players.¹⁵⁴

Because the state controls all licensed gaming agents who provide services, Delaware does not license private entities to operate Internet gambling in the same manner as Nevada and New Jersey.¹⁵⁵ Thus, Internet gambling in Delaware is only available through three websites operated in partnership by the Delaware State Lottery and 888 Holdings—the corporation hired by the state to provide Internet gambling services.¹⁵⁶ The stark differences in state regulation

as “all lottery games in which the player’s interaction with the game operated by the Office occurs over the Internet.”); *id.* § 4826(a) (2012) (under section 4826(a), only the operation of an “Internet Lottery” is authorized, which by definition must be operated by the State Lottery Office); *see also Delaware State Lottery Office Internet Lottery Rules and Regulations*, DELAWARE LOTTERY GAMES (effective Sept. 10, 2013), <http://www.delottery.com/pdf/InternetlotteryRules.pdf> (promulgating specific regulations for Delaware operation of Internet gambling).

¹⁵³ H.B. No. 333, 146th Gen. Assemb., (Del. 2012).

¹⁵⁴ *Id.*

¹⁵⁵ *See supra* p. 554 and note 152.

¹⁵⁶ *See* Brett Collson, *Delaware Selects 888 Holdings as Primary Online Gaming Provider*, POKER NEWS (May 3, 2013), <http://www.pokernews.com/news/2013/05/delaware-state-selects-888-holdings-as-primary-online-gaming-14912.htm>. Delaware operates the websites through its casino racetracks: Delaware Park, Dover Downs, and Harrington Raceway. *See About Us*, DELAWARE PARK ONLINE, <http://www.delawarepark.com/igaming/about.php> (last visited Nov. 26, 2014) (offering Delaware Park Online in partnership with the Delaware State Lottery and 888 Holdings as an Internet gambling website and stating that all games are lottery games controlled by the Delaware Lottery); *About Us*, DOVER DOWNS, <http://onlinegaming.doverdowns.com/about.htm> (last visited Nov. 26, 2014) (offering Dover Downs Hotel & Casino Online in partnership with the Delaware State Lottery and 888 Holdings as an Internet gambling website and stating that all games are lottery games controlled by the Delaware Lottery); *About Us*, HARRINGTON GAMING ONLINE, <http://www.harringtongamingonline.com/about.htm> (last visited Nov. 26, 2014) (stating that all games are controlled by the Delaware State Lottery).

illustrated above present a potential opportunity for the federal government to utilize the benefits of federalism and model a federal regulatory scheme after the superior states' approaches.

D. Internet Gambling Interstate Compacts

As exemplified by Nevada, New Jersey, and Delaware, regulatory schemes among states can differ widely.¹⁵⁷ The next step for states that have legalized and regulated Internet gambling is to expand their intrastate operations with interstate compacts in hopes of attracting a larger pool of players.¹⁵⁸ In September 2013, state officials acknowledged future plans to enter into such compacts: Nevada Governor Brian Sandoval had preliminary conversations with other states regarding compacts; Lisa Spengler, a spokeswoman for the New Jersey Division of Gaming Enforcement, confirmed that compacts will be considered in the future; and Delaware Finance Secretary, Thomas J. Cook, said that compacts will be looked into in 2014.¹⁵⁹ Only a few months after these acknowledgments, on February 25, 2014, the governors of Delaware and Nevada executed the first interstate Internet gambling compact.¹⁶⁰ The technology to implement multistate Internet gambling is still under development, but the execution of the agreement makes the activity legal.¹⁶¹

The Multi-State Internet Gaming Agreement establishes a governing body, the Multi-State Internet Gaming Board, to facilitate the implementation of interstate Internet gambling and oversee

¹⁵⁷ See *supra* Part IV.

¹⁵⁸ Pamela M. Prah, *N.J., Nev., Del wager on Online Gambling*, USA TODAY (Sept. 26, 2013), <http://www.usatoday.com/story/news/nation/2013/09/26/stateline-new-jersey-nevada-delaware-online-gambling/2875897/>.

¹⁵⁹ *Id.*

¹⁶⁰ *Multi-State Internet Gaming Agreement*, STATE OF DELAWARE OFFICE OF THE GOVERNOR 1 (Feb. 25, 2014), <http://governor.delaware.gov/docs/MultistateInternetGamingAgreement140224.pdf>.

¹⁶¹ See *id.* (declaring that federal laws leave states the ability to license and regulate Internet gambling); Aaron Nathans, *Delaware signs online poker compact with Nevada*, USA TODAY (Feb. 26, 2014), <http://www.usatoday.com/story/news/nation/2014/02/26/delaware-signs-online-poker-compact-with-nevada/5827947/> (citing Delaware Governor Jack Markell, stating that the agreement resolves the legality of intrastate online gambling).

member state adherence to the minimum regulatory standards the agreement sets forth.¹⁶² The agreement resolves tax rate discrepancies between member states by allowing individual states to set their own rates and methods of collection.¹⁶³ It further requires each state to collect revenue monthly and only allows each member state to collect revenue generated by players located within its boundaries.¹⁶⁴ Under the agreement, member states initially offer Internet poker, but they are free to offer other games for multistate play at their discretion.¹⁶⁵ The rapidity with which Nevada and Delaware drafted and executed an interstate compact for Internet gambling is an indicator that more such agreements will follow. These compacts represent simpler versions of regulation that proposed federal bills seek to accomplish.¹⁶⁶

V. FEDERAL REGULATION OF INTERNET GAMBLING

As demonstrated in the above section, state regulation of Internet gambling is a complex proposition with numerous differences among various states. Proposals for federal legislation regulating Internet gambling are similarly complex. Recent federal bills aiming for legalization and regulation of Internet gambling have gained limited traction, but they are nevertheless instructive for future efforts.

¹⁶² *Multi-State Internet Gaming Agreement*, *supra* note 160, at 5 (Article VII Governance of the agreement establishes the regulatory body). Spanning only two pages, the required minimum regulatory standards for member states contain exceedingly generalized terms, leaving member states significant latitude in *how* they meet the minimum standards. *Id.* at 12–13.

¹⁶³ *Id.* at 4–5.

¹⁶⁴ *Id.*

¹⁶⁵ *Id.* at 4.

¹⁶⁶ *Compare Multi-State Internet Gaming Agreement*, STATE OF DEL. OFFICE OF THE GOVERNOR (Feb. 25, 2014), <http://governor.delaware.gov/docs/MultistateInternetGamingAgreement140224.pdf> (the compact between Nevada and Delaware creates an overarching regulatory body to regulate interstate Internet gambling and enforce generalized minimum standards in a fourteen-page agreement), *with* Internet Gambling Regulation, Enforcement, and Consumer Protection Act, H.R. 2282, 113th Cong. 2013) (as referred to the H. Subcomm. on Crime, Terrorism, Homeland Sec., and Investigations, July 15, 2013) (recently proposed federal legislation accomplishes the same end with greater specificity and detail in a 134-page bill).

A. *H.R. 2282: Internet Gambling Regulation, Consumer Protection, and Enforcement Act of 2013*

The Internet Gambling Regulation, Consumer Protection, and Enforcement Act of 2013 (H.R. 2282),¹⁶⁷ sponsored by Representative Peter King, creates a federal regulatory body, the Office of Gambling Oversight in the Treasury Department, to establish licensing and quality control standards for states that decide to legalize Internet gambling.¹⁶⁸ As with the statutes in Nevada and New Jersey, this bill sets forth many regulatory necessities. Among other things, H.R. 2282 authorizes the Office of Gambling Oversight to: set the standards by which to approve or deny licenses; require independent inspection of hardware, software, communications equipment, and other devices used in Internet gambling to assure their integrity, accountability, and security; mandate oversight of licensing and operation; provide consumer protections; and enforce and prevent violations such as cheating and money laundering.¹⁶⁹ H.R. 2282 also delegates these regulatory responsibilities to any designated “qualified body.”¹⁷⁰ This means that approved state Internet gambling regulatory agencies would be able to license operators of Internet gambling, as long as the applicants meet the established minimum criteria.¹⁷¹ Appropriately, the bill includes adequate federal oversight of qualified bodies to ensure that they maintain the federally established standards of licensing.¹⁷²

¹⁶⁷ H.R. 2282, 113th Cong. (2013) (as referred to the H. Subcomm. on Crime, Terrorism, Homeland Sec., and Investigations, July 15, 2013), *available at* <http://www.gpo.gov/fdsys/pkg/BILLS-113hr2282ih/pdf/BILLS-113hr2282ih.pdf>.

¹⁶⁸ *Id.* § 104.

¹⁶⁹ *Id.* For a summary of H.R. 2282, see *CRS Summary*, THE LIBRARY OF CONGRESS, <http://thomas.loc.gov/cgi-bin/bdquery/z?d113:HR02282:@@D&summ2=m&> (last updated June 6, 2013).

¹⁷⁰ H.R. 2282 § 105(a)(1)(A)(ii)(I) (authorizing the Secretary to “at any time designate additional State agencies or regulatory bodies of Indian tribes as qualified bodies as deemed appropriate to carry out the goals of this Act, so long as they meet the criteria”).

¹⁷¹ *Id.* § 106(f)(1).

¹⁷² *Id.* § 106(d) (setting forth the standards for the investigation and determination of suitability of an applicant with which qualified bodies must adhere); *id.* § 106(f)(2)(A) (authorizing the Secretary to revoke a license issued by a qualified body if the Secretary has reason to believe that the recipient does not

H.R. 2282 addresses an important issue pertaining to the potential conflict with existing federal law regulating Internet gambling, such as the Wire Act and UIGEA.¹⁷³ H.R. 2282 proposes to add a clause to the UIGEA stating that “[t]he provisions of this subchapter . . . shall not apply to any bet or wager—(A) occurring pursuant to a license issued under *title I of the Internet Gambling Regulation, Enforcement, and Consumer Protection Act of 2013*, subject to *section 109 of that Act.*”¹⁷⁴ By operation of this amendment, H.R. 2282 would preempt the UIGEA. There is also a provision in H.R. 2282 that would amend the Wire Act for the same purpose.¹⁷⁵ These amendments are necessary because they clarify exactly how the different federal statutes that apply to Internet gambling will interact. Given the historical ambiguity of federal law related to Internet gambling, any new federal regulatory legislation should include provisions that resolve confusion surrounding existing law.

This lengthy bill is one of the most comprehensive proposals of its kind, detailing a complete federal regulatory scheme of all forms of Internet gambling.¹⁷⁶ It includes sections addressing sports betting, horseracing, and Indian gaming, all of which are sub-issues beyond the scope of this article.¹⁷⁷ H.R. 2282 is ambitious and has seemingly paid the price for its far-reaching goals; the bill is estimated to have only an eleven percent chance of getting past committee and a dismal two percent chance of being enacted.¹⁷⁸

meet the suitability requirements established under section 106(d); this power can undo improper license issuances and preserve the desired consistent minimum standards).

¹⁷³ *Id.* § 113.

¹⁷⁴ *Id.* § 113(d) (emphasis added).

¹⁷⁵ *Id.* § 113(f)(2) (amending the Wire Act such that H.R. 2282 would preempt it). H.R. 2282 also substantially alters the wording and definitions of the Wire Act, updating the language to reflect changes in technology since the Wire Act’s enactment in 1961. *Id.* § 113(f)(1).

¹⁷⁶ This is especially apparent when H.R. 2282 is combined with its intended counterpart, H.R. 3491: Internet Gambling Regulation and Tax Enforcement Act of 2013. See *infra* Part V.B.

¹⁷⁷ H.R. 2282 §§ 108–109, 113.

¹⁷⁸ See *H.R. 2282: Internet Gambling, Regulation, Enforcement, and Consumer Protection Act of 2013 Overview*, GOVTRACK.US, <https://www.govtrack.us/congress/bills/113/hr2282#overview> (last visited Aug. 15, 2014).

B. *H.R. 3491: Internet Gambling Regulation and Tax Enforcement Act of 2013*

The Internet Gambling Regulation and Tax Enforcement Act of 2013 (H.R. 3491),¹⁷⁹ introduced on November 14, 2013, is a counterpart to Representative King's H.R. 2282.¹⁸⁰ Sponsored by Representative Jim McDermott,¹⁸¹ H.R. 3491 provides for federal and state taxation of Internet gambling that H.R. 2282 would legalize and regulate.¹⁸² Perhaps the primary motivation for government legalization of Internet gambling is the promise of tax revenue, making the subject matter of the regulations within H.R. 3491 a necessity in any proposed federal regulatory scheme.¹⁸³

States that have legalized and taxed Internet gambling use the same basic gross revenue method of taxation, but H.R. 3491 takes a different approach.¹⁸⁴ Instead of basing taxation on gross revenue,

¹⁷⁹ Internet Gambling Regulation and Tax Enforcement Act, H.R. 3491, 113th Cong. (2013) (as referred to the H. Comm. on Ways and Means, Nov. 14, 2013), available at <http://www.gpo.gov/fdsys/pkg/BILLS-113hr3491ih/pdf/BILLS-113hr3491ih.pdf>.

¹⁸⁰ See James Carter, *Internet Gambling Regulation and Tax Enforcement Act of 2013 Introduced*, POKER STOP (Nov. 17, 2013, 2:20 PM), <http://www.pokerstop.com/internet-gambling-regulation-and-tax-enforcement-act-of-2013-introduced-3267>.

¹⁸¹ *Id.* Congressman McDermott (D) represents the 7th Congressional District of Washington, a state that has expressly prohibited all Internet gambling but has active Indian brick-and-mortar casino and state lottery industries. See 25 U.S.C. § 2701-21 (2012) (the Indian Gaming Regulatory Act authorizing Indian Tribes to regulate gaming activity on Indian land, including Indian land in Washington); WASH. REV. CODE § 9.46.240 (2006) (expressly prohibiting Internet gambling); WASH. REV. CODE § 67.70.010-906 (2002) (authorizing a state lottery).

¹⁸² H.R. 3491 §§ 4491, 4493.

¹⁸³ See Tony Nitti, *As New Jersey Prepares To Launch Internet Gambling, Congress Has Plan To Tax The Industry*, FORBES (Nov. 20, 2013, 7:36 PM) <http://www.forbes.com/sites/anthonyнити/2013/11/20/as-new-jersey-prepares-to-launch-internet-gambling-congress-has-plan-to-tax-the-industry/> (“Of course, anytime a once-blacklisted activity starts to become blessed by the federal government, one thing is sure to follow: taxes Continuing that trend, Congressman Jim McDermott (D-Wash) introduced a bill that would tax federally-sanctioned [I]nternet gambling should that day come to pass.”).

¹⁸⁴ See *supra* p. 547 and note 109 (Nevada taxing Internet gaming licensees' gross revenue at a rate not exceeding 6.75%); *supra* p. 551 and notes 132–134 (New Jersey taxing Internet gaming operators' gross revenue at the annual rate of

taxation under this bill is based on the amount of funds deposited by customers.¹⁸⁵ First, the federal government collects a four percent tax from each Internet gambling licensee on all customer deposits.¹⁸⁶ Next, H.R. 3491 authorizes a state Internet gambling tax of eight percent on all funds deposited by customers located in that state.¹⁸⁷ These taxes are collectable monthly on a pro-rata basis.¹⁸⁸ This tax procedure raises the concern that operators might impose fees on customer deposits or otherwise attempt to shift the tax burden to the customer. However, H.R. 3491 eliminates such loopholes, mandating that the tax “shall be the direct and exclusive obligation of the Internet gambling operator and may not be deducted from” the deposited amounts available to customers placing bets.¹⁸⁹ Notably, the bill gives Internet gambling operators a credit for taxes paid on any funds returned by the operators to customer bank accounts, reducing the tax’s scope to funds that remain deposited with licensees.¹⁹⁰

It is unclear whether a method of taxation on the basis of customer deposits or gross earnings is preferable; many variables change the debate.¹⁹¹ Furthermore, because state regulation of Internet gambling is in its infancy, estimates of Internet gambling revenue are questionable and certainly not to be relied upon.¹⁹²

15%); *supra* pp. 556–556 (Delaware collecting all Internet gambling gross revenue, less winnings paid to players, in its State Internet Lottery Fund and retaining about 44% of Internet slots revenue and 29% of revenue from all other games).

¹⁸⁵ H.R. 3491 §§ 4491(a)(1), 4493(b).

¹⁸⁶ *Id.* § 4491(a)(1).

¹⁸⁷ *Id.* § 4493(b). There is also an overseas gambling tax of 12% of all funds deposited by customers outside the United States. *Id.* § 4393(d).

¹⁸⁸ *Id.* §§ 4491(d), 4493(a)(1)–(2).

¹⁸⁹ *Id.* § 4491(a)(2); *see also* Nitti, *supra* note 183 (assuring the reader that Internet gambling licensees are prohibited from reducing the customer’s account by the taxes levied).

¹⁹⁰ H.R. 3491 § 4491(c).

¹⁹¹ For more analysis on Internet gambling taxation models, see Sanford I. Millar, *Taxation of Regulated Internet Gambling*, in REGULATING INTERNET GAMING: CHALLENGES AND OPPORTUNITIES, *supra* note 6, at 87.

¹⁹² LEGISLATIVE ANALYST’S OFFICE, *supra* note 116, at 2, 4–5. (Nevada estimates annual revenue at \$3 million; the Delaware State Department of Finance lowered its initial first-year revenue estimate of \$7.75 million to \$3.75 million; and

Regardless of these challenges, federal regulators should carefully examine gross revenue models implemented by states along with the customer deposit model proposed by H.R. 3491 while developing and implementing a taxation scheme for legalized Internet gambling.

C. *H.R. 2666: Internet Poker Freedom Act of 2013*

The Internet Poker Freedom Act of 2013 (H.R. 2666),¹⁹³ introduced on July 11, 2013 by Representative Joe Barton, has the primary goal of establishing a legalized federal regulatory scheme for Internet poker while leaving out other forms of Internet gambling such as blackjack, roulette, and other casino games.¹⁹⁴ This approach is procedurally similar to H.R. 2282 in that it creates a federal body, the Office of Internet Poker Oversight, to promulgate and enforce regulations. Substantively, however, it is significantly narrower in that it only regulates Internet poker.¹⁹⁵

Under H.R. 2666, the Office of Internet Poker Oversight may designate a state agency or regulatory body as a “qualified regulatory authority,”¹⁹⁶ enabling it to license operators of Internet poker, as long as the regulatory authority meets the prescribed minimum standards for qualification.¹⁹⁷ One of these standards is that the qualified regulatory authorities employ experienced staff and enforcement agents with sufficient sophistication and necessary resources to confront Internet poker regulatory issues.¹⁹⁸ Prior to the issuance of a license, H.R. 2666 specifically directs qualified regulatory authorities to make a determination of an applicant’s suitability, based on an investigation of the applicant and contents of

New Jersey lowered its initial annual revenue estimate from \$160–\$180 million to \$35–\$50 million).

¹⁹³ Internet Poker Freedom Act, H.R. 2666, 113th Cong. (2013) (as referred to the H. Subcomm. on Commerce, Mfg., and Trade, July 12, 2013), *available at* <http://www.gpo.gov/fdsys/pkg/BILLS-113hr2666ih/pdf/BILLS-113hr2666ih.pdf>.

¹⁹⁴ *Id.* § 103(b)(1) (establishing the Office of Internet Poker Oversight to carry out the functions assigned to the Secretary in H.R. 2666).

¹⁹⁵ *Compare id.*, with H.R. 2282 § 104 (creating the Office of Gambling Oversight to regulate Internet gambling, not limited to poker).

¹⁹⁶ H.R. 2666 § 103(c).

¹⁹⁷ *Id.* § 103(c)(1).

¹⁹⁸ *Id.* § 103(c)(2)(A).

the application.¹⁹⁹ This gives qualified regulatory authorities consistent procedures and standards to apply when deciding whether an applicant is suitable and has submitted a complete application. Finally, with regard to federal oversight of qualified regulatory authorities, the Office of Internet Poker Oversight may “take such action as [it] considers appropriate with respect to any qualified regulatory authority that appears . . . to be deficient or substantially less rigorous than other qualified regulatory authorities in the discharge of its responsibilities.”²⁰⁰ This oversight should be incorporated into an Internet regulatory scheme that delegates licensing and other regulatory authority to states so that each state may be held accountable for properly protecting consumers.

Similar to Nevada’s Internet gambling regulations, H.R. 2666 incorporates the prerequisite requirement that applicants must already operate a brick-and-mortar casino to be granted a license to operate Internet poker.²⁰¹ Thus, the bill favors the initial licensing of domestic applicants that may be more trustworthy to comply with regulations, given that they have a proven track record of compliance with gambling law. There is, however, an avenue for licensee hopefuls that do not operate brick-and-mortar casinos, such as foreign Internet gambling operators. H.R. 2666 provides that, two years after the date of the first license issuance, entities not operating a brick-and-mortar casino may be licensed if their entry into the Internet gambling industry is risk-free to the public.²⁰² This compromise provides a consumer safeguard by initially only licensing more trustworthy domestic operators, while leaving the door open for safe, foreign operators to enter the market after the two-year waiting period.

¹⁹⁹ *Id.* § 104(c)(1)–(2) (requiring investigation and describing the standards upon which suitability is to be determined); *id.* § 104(c)(2)(A)–(C) (an applicant’s suitability is based, among other things, on the applicant’s character, honesty, integrity, prior activities, and criminal record); *id.* § 104(b)(1)(A)–(G) (applications require many disclosures, including the applicant’s complete financial information, criminal and financial history, a description of the applicant’s plan for complying with requirements and regulations, and an agreement to be subject to jurisdictions of the courts in which the applicant has applied).

²⁰⁰ *Id.* § 103(d).

²⁰¹ *Id.* § 104(f)(1)(A)–(E); *see supra* p. 548 (explaining Nevada’s requirement).

²⁰² H.R. 2666 § 104(f)(2).

One unique aspect of this bill is that it prohibits the use of credit cards for Internet poker.²⁰³ Nowhere in the legislative findings is there any explanation for such a provision,²⁰⁴ nor do any other statutes regulating legal Internet gambling prohibit the use of credit cards for Internet gambling payments.²⁰⁵ This would seem to contradict the interest of the government in collecting revenue because credit cards are one of the easiest methods of payment for customers. Prohibiting their use forces customers to utilize less convenient means of payment, which could reduce online poker play and the revenue it generates for the regulating governments. On the other hand, credit card transactions can facilitate illegal money laundering in Internet gambling, a substantial area of concern for regulators of the industry.²⁰⁶

VI. FEDERAL REGULATORY PROPOSAL

The proposed bills and regulatory systems analyzed in the last section have unique qualities, each with their own strengths and weaknesses.²⁰⁷ A comprehensive federal regulatory proposal must incorporate the necessary regulatory attributes exemplified both in enacted state regulations and federal bill proposals, while also meeting the primary goals emphasized in nearly every jurisdiction's legislative findings on the topic of Internet gambling.

The first of such goals is to eliminate illegal Internet gambling through regulation of the activity.²⁰⁸ Other primary goals that a

²⁰³ *Id.* § 107(b) (“No licensee . . . may accept a bet or wager or payment for or settlement of a bet or wager that is transmitted or otherwise facilitated with a credit card.”).

²⁰⁴ *See id.* § 2(1)–(7) (enumerating the legislative findings without explicitly addressing the prohibition of the use of credit cards for payment).

²⁰⁵ In contrast, the Delaware Internet Lottery Rules and Regulations expressly allow monetary deposits by credit card. *See Delaware State Lottery Office Internet Lottery Rules and Regulations*, DELAWARE LOTTERY GAMES § 13.24.1 (effective Sept. 10, 2013), <http://www.delottery.com/pdf/InternetlotteryRules.pdf>.

²⁰⁶ *See generally* Stuart Hoegner, *Financial Transactions and Money Laundering*, in REGULATING INTERNET GAMING: CHALLENGES AND OPPORTUNITIES, *supra* note 6, at 187.

²⁰⁷ *See supra* Part V.

²⁰⁸ *E.g.*, NEV. REV. STAT. § 463.745 (2013) (legislative finding that an interactive gaming comprehensive regulatory structure will aid in law enforcement

federal regulatory scheme should accomplish include consumer protection, job creation, and collection of tax and licensing revenue.²⁰⁹ Finally, it is important for any new federal legislation to clarify existing federal law so there is no question as to the legality of Internet gambling activity.²¹⁰ These primary goals constitute the foundation for the construction of the following federal regulatory scheme.

First, the regulatory scheme must be designed as either a single provider model or a multiple license model. The single network model is similar to Delaware's state lottery system of regulation.²¹¹ The Delaware State Lottery Office controls all Internet gambling operated by the "agents" it licenses and controls.²¹² This system gives the government extreme control over the industry, as patrons must gamble exclusively via government-operated websites.²¹³ This is different from the multiple license model approach used in Nevada and New Jersey, where the states licenses multiple entities to operate

efforts against unauthorized interactive gaming); N.J. STAT. ANN. § 5:12–95.17 (West 2014) (legislative finding that regulation of Internet gaming will provide regulators and law enforcement the resources to restrict and stop the illegal Internet gambling market).

²⁰⁹ Internet Gambling Regulation, Enforcement, and Consumer Protection Act, H.R. 2282, 113th Cong. (2013) § 101(a)(1) (as referred to the H. Subcomm. on Crime, Terrorism, Homeland Sec., and Investigations, July 15, 2013), *available at* <http://www.gpo.gov/fdsys/pkg/BILLS-113hr2282ih/pdf/BILLS-113hr2282ih.pdf> (finding that "Internet sites offering Internet gambling have raised consumer protection and enforcement concerns for Federal and State governments, as such Internet sites are often run by unknown operators located in many different countries, subject to little or no oversight, and have sought to attract customers from the United States"); H.R. 2666 § 2(7) (finding that "[s]uch a program would create new industry within the United States creating thousands of jobs and substantial revenue for Federal, State, and tribal governments").

²¹⁰ *See* H.R. 2822 § 101(a)(7) (finding that "[f]ederal law needs to be updated to make clear its relationship to Internet gambling to strengthen enforcement and to ensure an effective Internet gambling enforcement structure . . .").

²¹¹ *Online Gambling Legalization is Happening NOW*, PERKINS COIE LLP (July 2012), <http://www.perkinscoie.com/images/content/2/7/v2/27481/12-08-all-gambling-onesheet-final.pdf>.

²¹² *See generally* Delaware State Lottery Office, INTERNET LOTTERY RULES AND REGULATIONS (effective Sept. 10, 2013), <http://www.delottery.com/pdf/InternetlotteryRules.pdf>.

²¹³ *Id.*

private Internet gambling websites.²¹⁴ This is closer to a privatized, free-market approach because there is regulatory oversight of a market with competing Internet gambling networks.²¹⁵ A federal regulatory scheme will have to be modeled after one of these approaches.

Next, the regulation must address the issue of licensing Internet gambling operators, service providers, technology providers, and any other entities that participate in the industry. Licensing regulations can differ widely depending on their breadth, depth, level of review, criteria, and standards.²¹⁶ One common feature of Internet gambling licensing regulations that a federal regulatory scheme must consider is the requirement that applicants have operated a brick-and-mortar casino.²¹⁷ Another important licensing issue related to criteria is whether operators that facilitated illegal Internet gambling in the United States will be eligible for a license.²¹⁸ In making these important licensing decisions, the federal government must balance the cost of imposing burdensome licensing requirements with the benefits of the regulatory goals that they seek to meet.²¹⁹

An Internet gambling regulatory system should also provide for the fees and taxes that accompany licensing and operation of Internet gambling. There are two general approaches to the taxation of Internet gambling: taxation of gross gambling revenues or taxation of gross deposits.²²⁰ Nevada, Delaware, and New Jersey all use a gross

²¹⁴ See *supra* Part IV.A–B.

²¹⁵ *Online Gambling Legalization is Happening NOW*, *supra* note 211.

²¹⁶ CABOT & PINDELL, *supra* note 6, at 11–12 (breadth is the extent to which regulations require entities to obtain licenses; depth is the extent to which people within an applying entity are investigated in the licensing process; level of review refers to the intensity of the investigation; criteria are elements that the government considers when making licensing decisions; and standards entail the level of rigidity with which the criteria are applied).

²¹⁷ See *supra* p. 551 (New Jersey’s regulations incorporate this general requirement); *supra* p. 548 (Nevada’s regulations incorporate this general requirement); *supra* p. 566 (H.R. 2666 would also include this general requirement).

²¹⁸ CABOT & PINDELL, *supra* note 6, at 48.

²¹⁹ *Id.* at 11.

²²⁰ Sanford I. Millar, *Taxation of Regulated Internet Gambling*, in REGULATING INTERNET GAMING: CHALLENGES AND OPPORTUNITIES, *supra* note 6, at 87, 90–92.

revenue approach, whereas the proposed H.R. 3491 would tax gross deposits.²²¹ Each system has its benefits and drawbacks; however, the deposit model seems more efficient for taxation of multiple jurisdictions.²²² Another important consideration is the distribution of tax revenue between the federal government and the state governments.²²³ A federal regulatory scheme setting forth a uniform system of taxation would provide greater consistency and predictability to entities paying taxes and governments collecting them.²²⁴

The final important provision in a federal regulatory statute will clearly define the way in which new federal legislation interacts with the Wire Act and the UIGEA. As part of the federal regulatory scheme, the older statutes should be amended so that the new legislation preempts them.²²⁵ This fulfills the important goal of clarifying existing federal law, leaving no doubt as to the state of federal law regarding Internet gambling.

VII. CONCLUSION

The benefits of legalizing and regulating Internet gambling are enumerated throughout the legislative findings of state statutes.²²⁶ One of the most commonly cited reasons is that, regardless of the law, consumers will find ways to gamble illegally over the

²²¹ See *supra* pp. 550–548 (Nevada); see *supra* p. 551 (New Jersey); see *supra* pp. 30–31 (Delaware); see *supra* p. 561 (H.R. 3491).

²²² Sanford I. Millar, *Taxation of Regulated Internet Gambling*, in REGULATING INTERNET GAMING: CHALLENGES AND OPPORTUNITIES, *supra* note 6, at 91.

²²³ See *supra* p. 561.

²²⁴ Sanford I. Millar, *Taxation of Regulated Internet Gambling*, in REGULATING INTERNET GAMING: CHALLENGES AND OPPORTUNITIES, *supra* note 6, at 87, 90–92 (contrasting different models of taxation with regard to the differing levels of consistency and predictability in the taxation they provide). For more information and analysis of Internet gambling taxation models, see generally *id.*

²²⁵ See *supra* p. 559 (the proposed amendments provided in the Internet Gambling Regulation, Enforcement, and Consumer Protection Act of 2013 have this exact effect).

²²⁶ E.g., *supra* p. 551 (New Jersey's legislative findings on the benefits of legalizing and regulating Internet gambling).

Internet.²²⁷ Thus, the federal government should step in and regulate the industry, protecting consumers while benefitting from an added source of tax revenue and job growth.²²⁸ This reasoning, however, is becoming outdated, given that *legalized* Internet gambling is rapidly growing among the states.²²⁹ Instead, federal regulation is now needed to clarify existing federal law and to set forth minimum standards to ensure that legal Internet gambling is appropriately regulated by the states.

The future of Internet gambling in the United States is rapidly developing, and at least ten states are expected to consider bills that would legalize Internet gambling.²³⁰ States are taking it upon themselves, in the absence of federal regulation, to legalize Internet gambling.²³¹ The tax revenue states could obtain from regulating this activity is significant; in New Jersey alone, the Internet gambling market is projected to generate \$262 million in gross gambling revenue in 2014.²³² There is little doubt that states considering legalization are privy to these projections.

A federal regulatory scheme that establishes and enforces detailed minimum standards and procedures for the regulation and licensing of Internet gambling would go far to ensure the legitimacy of all licensed operators and secure the future of Internet gambling. As United States Representative Lee Terry said during a hearing of the

²²⁷ Americans spent an estimated \$2.6 billion on illegal, offshore Internet gambling in 2012. Prah, *supra* note 158.

²²⁸ *E.g.*, Internet Poker Freedom Act, H.R. 2666, 113th Cong. § 2(6)-(7) (2013) (as referred to the H. Subcomm. on Commerce, Mfg., and Trade, July 12, 2013), available at <http://www.gpo.gov/fdsys/pkg/BILLS-113hr2666ih/pdf/BILLS-113hr2666ih.pdf>.

²²⁹ Niraj Chokshi, *At Least 10 States Expected to Consider Allowing Online Gambling This Year*, WASH. POST (Feb. 5, 2014), <http://www.washingtonpost.com/blogs/govbeat/wp/2014/02/05/at-least-10-states-expected-to-consider-allowing-online-gambling-this-year/>. States considering legislation include California, Colorado, Hawaii, Iowa, Louisiana, Massachusetts, Mississippi, and Pennsylvania, along with consideration of expanded Internet gambling in Illinois and New Jersey. *Id.*; see also *supra* Part IV.

²³⁰ Chokshi, *supra* note 229.

²³¹ *Id.* Federal inaction is expected to continue this year because it is an election year and “virtually all politically controversial subjects, including Internet gambling, will be seen through the risk-averse lens of re-election.” *Id.*

²³² *Id.*

House Subcommittee on Commerce, Manufacturing, and Trade on December 10, 2013, “[w]hile unfettered online gaming here in the U[nited] S[tates] is surely not the ideal, absent a clear mandate from Congress, we risk exposing our constituents to an environment where a ‘race to the bottom’ could present itself.”²³³ The time has come for the federal government to mitigate that risk.

²³³ Tom Risen, *Gaming Companies Bet on Internet Poker Returning to U.S.*, U.S. NEWS & WORLD REPORT (Dec. 11, 2013, 6:20 PM), <http://www.usnews.com/news/articles/2013/12/11/gaming-companies-bet-on-internet-poker-returning-to-us>.