

Why Internet Gaming Comes up Snake Eyes for U.S. Processors

Ed McKinley

With poker and other games soaring in popularity, online betting looks like a juicy market. But prosecutorial zeal at both federal and state levels has made this a market for offshore casinos and foreign processors.

Hit shows like the World Series of Poker have helped make such games of chance hip and hot, particularly among younger adults, and Internet gambling is riding the wave. There are approximately 2,000 gambling sites, all operating abroad, and they are expected to rake in \$10 billion in revenue worldwide this year, up 40% from 2004, according to published reports. Half of that take comes from gamblers in the U.S. That may sound like a slot machine poised for a big payout for online transaction processors. Trouble is, online gaming is about as popular as Osama bin Laden these days with the feds, and that's scaring away most processors and card networks.

"The risks of operating an online casino here are tremendous," says Lawrence G. Walters, a partner in a national law firm that represents casinos and companies that provide casino services. As it turns out, no specific federal laws prohibit online gambling. But Walters and other legal experts point out that the U.S. Justice Department considers Internet gaming a violation of the Federal Wire Act, punishable with two years in prison for each violation.

The Online Casino Market: A Snapshot	
Number of Gambling Sites:	2,000
Number operating in the U.S.:	Zero
Projected revenue for these sites in 2005:	\$10 billion worldwide
Increase over 2004:	40%
Proportion of the take from the U.S. gamblers:	50%

Source: Published reports

Multiple violations of the Wire Act could trigger federal racketeering laws, which carries penalties of decades in jail, forfeiture of assets, and six-figure fines, Walters says. So far, he concedes, federal prosecutors have threatened to use the racketeering laws against Web gambling operations but have stopped short of making it the basis for any cases.

Federal prosecutors' interpretation of the 44-year-old law is not without controversy, as some experts point out the statute only prohibits sports betting over state and international borders, not all gambling activity, like today's red-hot poker mania. Indeed, three federal courts have held the law is aimed only at sports bets.

Few casinos, however, want to test Justice's stand in court. And, lest anyone rely too much on that argument, federal prosecutors also use the Interstate Transportation of Wagering Paraphernalia Act against

Web gambling operations, Walters says, noting that the law empowers the government to seize computers as gambling devices.

The result is a depressing patchwork of opportunities in the U.S. for online casino operators and processors that might want to handle their betting traffic. I. Nelson Rose, a law professor at Whittier Law School, Costa Mesa, Calif., and author of a number of books on the legal ramifications of gambling, puts it this way: “If they were here, casinos would be closed down. There is no online poker or lottery from the United States. Betting on horse racing has been made illegal by Congress, but it’s up to each individual state so you can bet on horse racing from many states. Even bingo is not legal but it’s fairly popular because there are free versions, where you don’t pay anything but you’re subjected to advertising.”

Offshore Processors

Although Internet casinos can’t operate legally in the United States, Americans own some of the offshore online gambling halls, says Steve Mott, chief executive of BetterBuyDesign, a Stamford, Conn.-based consulting firm. Rose says such owners often feel exiled from the United States, afraid to return home lest they face prosecution here.

Nor are states any less rabid against Internet gaming than the feds. In 1997, for example, Minnesota Attorney General Hubert “Skip” Humphrey III, son of former vice president Hubert Humphrey, successfully argued that a Nevada man who arranged sports bets online between individuals had to appear in Minnesota to defend himself against online gambling charges. The Nevada man withdrew from the business, Rose says. Claims of false advertising formed the basis of the celebrated case, he says.

In 2002, New York Attorney General Elliot Spitzer forced PayPal, the nation’s largest online payment service, out of the business of processing online gambling transactions for residents of New York State and imposed penalties of \$200,000 to cover the cost of the state’s investigation. PayPal has since stopped handling online gambling transactions entirely.

Walters says U.S. payment processors that handle bets could face federal charges of conspiracy or aiding and abetting other violations. “The government relies on those laws when they need to catch somebody into the net of conspiracy and hit somebody on the outer fringes of the activity,” he says, adding that no federal law specifically prohibits processing bets.

That legal status could change, however. Congress is considering a bill introduced by Sen. Jon Kyl, R-Ariz., called the Unlawful Gambling Funding Prohibition Act, that would make the processing of gambling transactions by payment processors and credit card companies illegal, Walters says.

Such legislation would further secure the position of offshore payment processors, many of them operating in the British Commonwealth, where online gambling is legal, says Rose. He cites FirePay and Neteller as two of the biggest online gambling payment processors, but both failed to return phone calls and e-mail messages seeking comment for this article.

Meanwhile, like payment processors, most American credit card issuers have exited the Internet gambling business since 2002. The issuers refuse to authorize transactions involving merchant numbers assigned to Web gambling houses, says consultant Mott. Rose says issuers have made that decision even though no law clearly prevents using cards for online gambling.

Bankers often shy away from what many might consider the impropriety of gaming, says Rose. “Bankers are conservative,” he says. “They don’t want their children to come home and say, ‘Daddy, I heard you were indicted as a racketeer.’”

Card issues also may want to avoid chargebacks, fearing that unscrupulous cardholders might run up online gambling debts with a card and then claim the plastic was lost or stolen, says Rose.

Prepaid Wallets

The card associations and issuers acknowledge their customers’ identification with the “romance” of gambling by offering affinity cards with the names and images of famous casinos. In the fine print they note that cardholders can’t use the cards for Internet gambling, says Rose.

Despite the legal dust-ups surrounding online betting, America’s Internet gamblers thus far have remained outside the fray. Few states have made it a crime to place a bet on the Internet, says Rose. The federal government, perhaps recalling the futility of trying to keep the nation dry during Prohibition, has chosen not to pursue the customers of online casinos.

Charging online gamblers with aiding and abetting illegal gambling doesn’t work as a legal theory, says Rose. He likens it to the faulty argument that someone who buys illicit drugs is aiding and abetting a drug seller and is, therefore, guilty of selling drugs himself. “There have to be some limits on the law,” he says.

The lack of legislation dealing directly with Internet gambling may be due to the relative newness of the Web. Probably the oldest online gambling sites are sports books, Rose says. Some claim to date back to the late 1980s, he says, but in those days merely advertised online and took bets by phone.

Sitting at a computer and looking back over his old columns, Rose notes that he began writing about online wagering in the early 1990s. By 1995, online gambling had become a hot legal issue, he says, and the industry became big by the late ’90s.

By 1998, pundits were predicting that online gambling, which then brought in about \$1 billion annually, soon would reach \$100 billion a year, growing to one-fifth the size of land-based gambling, Rose says. Growth slowed dramatically, however, when online casinos hit legal snags and U.S.-based businesses pulled out, he says.

The image shows a screenshot of the CasinoEuro.com website. At the top, the logo 'casino.com' is prominent, along with 'CasinoEuro.com' and a '+ 30% DEPOSIT BONUS EVERY MONTH' offer. A 'PLAY NOW' button is visible. The navigation bar includes links for 'Play Blackjack', 'Play Slots', 'Play Video Poker', 'Play Craps', and 'Play Roulette'. A large central banner for 'PIGGS PEAK CASINO' features a '\$100 FREE' offer and a 'CLICK HERE TO GAMBLE ONLINE' button. To the left, a sidebar lists 'Online Casinos' (About Online Gambling, Getting Started, System Requirements, Index, Free Casino Software, Feeling lucky?, Trusted Security, Banking, Mobile Gaming) and 'Games' (Play for Fun, Blackjack, Slots, Video Poker, Roulette, Craps). Below that are 'Rules & Strategies' (Blackjack, Caribbean Stud, Craps, Poker). On the right, a 'Featured Casino' section highlights 'Reef Club Casino' with a '\$100 FREE' offer and a 'CLICK HERE' button. The website also displays '16 LANGUAGES' and '13779 Players Online'.

Sites like this tap into America's gambling craze, but currently there's no jackpot here for U.S. processors.

Today, the offshore casinos offer gamblers the option of funding prepaid wallets operated by offshore payment processors. The processors use quick searches of multiple databanks to ask online gamblers questions that can go a long way in establishing identity. Correct and incorrect statements are mixed to throw off people posing as someone they are not, says Mott.

Odd Situation

Sometimes, as a means of identification, processors put a small sum in an online gambler's account, say 26 cents, and ask the gambler how much was deposited. Programmers also are perfecting software programs that can trace the location of potential online gamblers. "You probably have more guarantees doing an online gambling financial transaction than if you walked into your own bank or use an ATM," says Rose.

Online gamblers have the option of dipping directly into their bank accounts through processors like Toronto-based UseMyBank Services Inc., says Joseph Iuso, chief executive of the 2-year-old company. UseMyBank customers give the company the information needed to gain access to accounts through online banking systems, but the service uses the numbers once and does not store them on its servers, Iuso says.

He also notes that debit payments help online gamblers remain more responsible than they might be if they use credit cards to borrow money to wager. UseMyBank is expanding from Canada to the United States and Europe. It's now used mostly to pay for online gambling and dating services.

However online gambling is funded, though, it remains illegal in the United States, a situation that some find odd since gaming has become legal at so many land-based casinos here. Legalizing Internet wagering would allow the government to weed out dishonest gambling houses and ensure better odds for the gamblers, besides opening up lucrative opportunities for American business, observers point out. "You can go to Las Vegas or Atlantic City and draw money off your credit card to gamble all day long," says Mott, "but for some reason you can't do it online."

Until that changes, processors eyeing a transaction jackpot in Web casinos will shy away, afraid to bet against the house.