



Race Track Industry Program

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### WTO — The Big “Do-Over”? And How to Regulate Internet Gaming — Department Of The Treasury Rules

#### Speakers:

**Joe Baressi**, Financial Services Project Leader, Federal Reserve Board of Governors  
**Bruce Zagaris**, Attorney, Berlinger Corcoran & Rowe LLP

**MR. STEVE BARHAM:** Please turn off cell phones or put them on vibrate. First thing I would like to do is thank our sponsor for this panel, Racing and Gaming Services. Each of the speaker's bios are in the back of the program, I'm not going to spend any time going through those, you can read them for yourselves.

This panel is really a combination of two topics, one is a WTO or as Wendy Davis called it when we were talking about it, “The Big Do-Over,” and how to regulate the Internet gaming, which really deals with the Unlawful Gambling Enforcement Act.

With us we have Bruce Zagaris and Joe Baressi, probably mispronounced the name, sorry. And dealing with bureaucrats, which I used to be one of, and lawyers, which I've had a lot of experience dealing with both working for me and working for and yelling at me, true to form, these guys have switched positions. So they've taken control of everything. So with that, Joe?

**MR. JOE BARESSI:** Hi everyone, my name is Joe. I'm with the Federal Reserve Board of Governors. I am here to talk to you today about the Unlawful Internet Gambling Enforcement Act. I prepared handouts and they are going to be available on the Web site after the conference, and there are hard copies of the handout by the door. I don't — it's just words, so I don't think that it's necessary to have them up there, I'm going to speak to the words on the handouts very closely.

So the Unlawful Internet Gambling Enforcement Act was passed in October of last year. It did a number of things and did not do a number of things and people have, I think, gotten confused as to what the Act did and did not do. What I would call the core of the Act was to create a new crime under federal law and that crime is for a business engaged in gambling, a gambling business to accept payments in connection with unlawful Internet gambling.

So let me sort of break that out a bit. You have a ton, prior to the October Act; you have a ton of preexisting state and federal gambling law, which I am not an expert on. And that gambling law determines what, that preexisting gambling law determines what gambling is legal and what gambling is illegal. The October Act, the Unlawful Internet Gambling Enforcement Act comes along and says, "Stick with that preexisting law to determine what's legal or illegal, if it's illegal, here's a new crime." It's a new crime to accept payments in connection with gambling, Internet gambling that is illegal under that preexisting law. And the perpetrator of that crime would be a gambling business as opposed to a person or a financial institution, a bank. Being with the Federal Reserve, my typical audience or customers or what have you are banks, not horse racing.

So crime, that's the core of the Act, the other thing that the Act did and the reason that I'm here is the Act also instructed the Treasury, the United States Treasury Department, and the Federal Reserve Board of Governors, to write civil regulations that will apply to participants and payment systems, basically banks, well, broader than banks, I'll get to that. So you have the criminal aspects of the Act, and then you have the civil right regulations aspect of the Act, and so the Act instructs the Federal Reserve and the secretary to write regulations regarding payments related to Internet gambling.

So the crime aspect applies to business, gambling business, the regulatory aspect, the reason that I'm here is participants in financial systems and what do those participants and financial systems have to do? Under the Act they have to develop policies and procedures reasonably designed to identify and block or otherwise prevent or prohibit payments in connection with unlawful Internet gambling. That's a long-winded, that's a long phrase but because it is a series of ors, identify and block, or prevent or prohibit, it actually is very broad, some might say non-informative in terms of what the financial institutions policies and procedures are supposed to do. And so that is where the Federal Reserve and the Treasury come in. The Act also instructed us to provide examples of what such policies and procedures would be. I am not going to go into detail about what our proposed rule said in terms of its examples of policies and procedures for financial institutions. Basically, I can't because we, the Federal Reserve and the Secretary of the Treasury are currently within our comment period on the proposed regulations. The comment period opened at the beginning of October, October 2007, and the comment period closes on December 12<sup>th</sup>, 2007, so in about a week, in exactly a week. In the handout you will see links on where to go if you want to see the comments that we received, if you want to submit a comment or if you want to read our proposed regulations.

At a high level, what the proposed regulation does is it follows the Act's instructions closely. And a lot of the comments that we've received so far go to the wisdom of the Act itself. Basically, comments saying, "We think the Unlawful Internet Gambling Enforcement Act is not good," which agree or disagree, as a regulator, I can't do anything about what the Act says. Basically, Congress is sort of God to an agency, and Congress passes a law and then as a bureaucrat, as a person at the agency, I write regulations, or we write regulations that implement the Act. Our regulations can clarify where the Act is unclear, but our regulations cannot contradict what the Act says. Our regulations cannot say anything that is inconsistent with what the Act says. So I, in phone conversations, e-mails, what have you, that's the point that I try to get across to people, make sure that your complaints or thoughts to the Board and to the Treasury go to the regulations, the scope of our authority within the regulations as opposed to what Congress did in the Act, because as a regulator I can't change what Congress did. Only Congress can change what Congress did.

So within that framework, basically what our proposed rule does is it designates the payment systems, so the Act says, "Financial transaction provider participants in payment systems are supposed to develop these policies and procedures reasonably designed to identify and block or otherwise prevent or prohibit unlawful Internet gambling transactions. So what our proposed rule does is designate payment systems and those payment systems are the automated clearinghouses, checks, cards, debit or credit cards, wire transfers, and money transmitting businesses.

To sort of clarify a bit what each of those are, the automated clearinghouse system is often shortened to ACH, that's an electronic clearing network run by the Federal Reserve, a typical example of what it's used for is direct deposit of people's paychecks. That is one of the payment systems. Checks, I think most people are familiar with. Cards, I think most people are familiar with, debit, credit cards. Wire transfer and money transmitting business are two things that people seem to get confused on. The way payments law uses the term wire transfer, it's kind of a term of art, it refers to basically Fed wire or chips payments, which are, Fed wire is a network between banks, operating between banks, run by the Federal Reserve. Chips is a private sector, very similar network run by banks and, again, it's between banks. So basically the way that I use the term wire transfer, it's referring to a real-time electronic payment between two banks. Whereas, in sort of the public, the term wire can be used to refer to a Western Union payment. Under the terms of our regulations, a Western Union is a money transmitting business. So the regulations that apply to a money transfer, the proposed regulations that would apply to wire transfer don't apply to Western Union. Similarly, the proposed regulations that apply to Western Union-type entities would not be the same as what applies to Fed wire payments.

Other examples of money transmitting businesses are PayPal; really any online payment system that is not operated by a bank would basically be a money transmitting business.

Are there any questions about the payment systems, what they are? Okay.

The last thing that I'll say before I turn it over to Bruce, the Act required the agencies to exempt certain payment systems and or restricted transactions. It required the agency to exempt certain payment systems if the agencies found that it is not reasonably practical to identify and block or otherwise prevent or prohibit restricted transactions. So that's a very broad exempted authority that it gave to us and we used it, we didn't exempt any payment systems, any of those payment systems that I mentioned in their entirety, so none of them are exempt, but we did exempt certain participants within those payment systems. And in terms of comments from the public, that's really, to my mind, what I would be interested to hear, what people think in terms of what they think is reasonable for financial institutions to do, bank or non-bank, you know, Citigroup, Western Union and so on. What they think it's reasonable to do, did we get the exemptions right in terms of saying, "In these instances it's not reasonably practical for you to do anything?"

And like I said, in terms of where we go from here, the comment period closes on December 12<sup>th</sup>; we the Federal Reserve and the Treasury are required to publish final rules. So we've issued our proposed rules, we've requested comments, time period for submitting comments closes on December 12<sup>th</sup>, we are required to publish final rules as desirable or non-desirable as they may be, as desirable or non-desirable as the Act may be. We are required to publish our final rules and in fact the deadline, we are way behind, the deadline, we were supposed to publish our final rules by July 12<sup>th</sup> of 2007. So we are going to miss that by close to a year. But anyway, where I'm going with that is this topic is not done, so comments, whether formally through the comment process as per the last slide in my handout, or just through phone, e-mail type stuff, or talking with me after this session, we are a long way from finished on this topic.

And with that, I'm going to turn it over to Bruce who is going to talk about the WTO aspects of Internet gambling and I'll — I think that we're going to have time at the end of our session to take questions and I will be around after the session time has ended to talk with any of you.

**(Applause)**

**MR. BRUCE ZAGARIS:** Good morning. First, just to give you a little bit of background on where I'm coming from on this issue, I've worked in the past for an Internet gaming association on helping them formulate their international strategy. I've also worked on some due diligence for joint venture transactions between Internet gaming companies. And I've also done a lot of work over the years for small governments that are involved in international trade and services. So that is essentially my background.

What I'm going to do is look at four different areas of this issue; one is the background to the dispute which involves the case that Antigua and Barbuda brought. It also involves the Unlawful Internet Gaming Enforcement Act of 2006, but since Joe has covered the regs and has covered that well, I'm going to skip

over most of that. I also have PowerPoint's and some additional materials that are, you can get afterwards or you can get from the Web site. Then I'm going to talk secondly about what the potential U.S. options are as a result of what's happened with the WTO. Then I'm going to talk about the Article Twenty-One procedures, which happened when, as a result of the adverse decision on the WTO, the U.S. essentially withdrew its commitment on gaming services including Internet gaming services, and that has started a whole new procedure now that pits the U.S. against, not just Antigua and Barbuda, but about 10 countries including the EU. And then I'm going to speak briefly about some of the bills that are now pending in Congress and then finally I'm going to talk about what I see in the future and what some of the alternatives are for the horse racing industry.....**Other terms, concepts and keywords contained in the balance of this transcript are:** Internet gaming, Article Twenty-One, compensatory adjustment, Frank Bill, Berkley Bill, H.R. 2140, H.R. 2610, H.R. 2046, Internet Gambling Regulation and Enforcement Act, revenue, credit card industry.....If you desire a full transcript contact [bprewitt@ag.arizona.edu](mailto:bprewitt@ag.arizona.edu)

